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No. _____

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1992

AMERICAN NATIONAL BANK & TRUST COMPANY, - - - - - - - - - Petitioner

versus

H. C. HANSON,
VIRGINIA HANSON,
H. C. HANSON CONSTRUCTION COMPANY, INC., and
CONSTRUCTION ENGINEERS, INC., - Respondents

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF KENTUCKY

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March 17, 1993

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QUESTIONS PRESENTED

1. Whether the trial court denied American National Bank & Trust Company ("American National") its rights to due process by permitting the jury to award punitive damages when it had refused to instruct the jury that it had directed verdicts for American National on the inflammatory issues of infliction of emotional distress, physical injuries, and fiduciary duty.

2. Whether the trial court denied American National its rights to due process by denying it a post-trial review in accordance with acceptable standards as set forth in *Pacific Mut. Life Ins. Co.* v. *Haslip*, 499 U.S.___, 111 S.Ct. at 1032 (1991).

3. Whether the Kentucky Supreme Court denied American National its rights to due process by interpreting *Haslip* to require only a trial court review of punitive damage awards under the "first blush" test and appellate review of only errors of law made by the trial court.

4. Whether by reversing the decision of the Kentucky Court of Appeals, holding the award of punitive damages to be excessive, the Kentucky Supreme Court denied American National its rights to substantive due process.

PARTIES TO THE PROCEEDING

The Petitioner, American National Bank & Trust Company ("American National" or "Bank"), is a wholly-owned subsidiary of First Kentucky National Corporation ("FKNC"), which is a wholly-owned subsidiary of National City Corporation ("NCC").

The Respondents are H. C. Hanson Construction Company, Inc. ("Hanson Construction" or "Company"), Construction Engineers, Inc. ("Construction Engineers"), H. C. Hanson ("Hanson"), and Virginia Hanson (collectively "Hansons").

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v.

H. C. HANSON,
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H. C. HANSON CONSTRUCTION COMPANY, INC., and
CONSTRUCTION ENGINEERS, INC., - - - *Respondents*

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF KENTUCKY

Petitioner hereby petitions for a Writ of Certiorari to review the decision of the Supreme Court of Kentucky in this case.

OPINIONS BELOW

The decision of the Supreme Court of Kentucky (Appendix, *infra*, pp. 1a-16a) is reported at 844 S.W.2d 408 (Ky. 1992). That decision affirmed in part and reversed in part a decision of the Court of Appeals of Kentucky that was not reported. It is reprinted in Appendix, *infra*, pp 17a-34a. The decision of the Court of Appeals of Kentucky affirmed in part and reversed in part an amended judgment of Warren Circuit Court, entered March 7, 1989, pursuant to a jury verdict rendered on January 25, 1989. The

amended judgment of Warren Circuit Court (Appendix, *infra*, pp. 35a-40a) denied the Petitioner's motions for new trial, judgment notwithstanding the verdict and/or remittitur.

JURISDICTION

The decision of the Supreme Court of Kentucky was rendered December 17, 1992. No petition for re-hearing was sought. The jurisdiction of this Court is invoked pursuant to the provisions of 28 U.S.C.A.§1257(a) (West Supp. 1992).

CONSTITUTIONAL PROVISION INVOLVED

The Fourteenth Amendment to the Constitution of the United States provides in part: "No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any state deprive any person of life, liberty, or property, without due process of law. . . ."

STATEMENT OF THE CASE

This Petition presents for review the first case from the Kentucky Supreme Court which affirmed an extremely large award of punitive damages based on its interpretation of the review standards approved in *Pacific Mut. Life Ins. Co.* v. *Haslip*, 499 U.S. __, 111 S.Ct. 1032 (1991).

The jury awarded the Hansons $1,065,000.00 in compensatory damages and $5,775,000.00 in punitive damages. The Kentucky Court of Appeals affirmed the compensatory damages but reversed the punitive damages as excessive. The Supreme Court of Kentucky reversed that part of the decision of the Kentucky Court of Appeals respecting punitive damages and reinstated the jury's award of punitive damages in its entirety. By so doing, it failed to apply, or

misinterpreted, the due process standards approved in *Haslip*.

Hanson, a degreed engineer, formed Hanson Construction and Construction Engineers to engage in highway bridge construction. During the mid-1970's, Hanson Construction became a customer of American National. From 1982 through 1985, Hanson Construction lost [$403,359.00]. As the losses increased, stockholder equity dropped and the Company's debt to American National rose. Hanson admitted that the Company kept operating only through monies borrowed from American National. By 1985, American National's loans to Hanson Construction were classified.[1]

In February 1985, American National was purchased by FKNC. Employees of First National Bank of Louisville, another subsidiary of FKNC, were assigned to American National to assist in its operations. In June 1985, one of those employees, Tom Gurbach, a management trainee, was asked to review Hanson loans.

Hanson Construction had seven (7) outstanding notes with American National, including a line of credit (total debt of $632,848.00). Hanson was personally obligated on the entire debt. His wife, Virginia Hanson, was personally obligated on up to $300,000.00 of Company debt.

As a part of his review of Hanson Construction, Gurbach prepared a Memorandum dated July 8, 1985. That Memo-

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[1] Classified loans are loans that are "characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected." (Joint Statement of the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Conference of State Bank Supervisors on "The Classification of Assets in Bank Examination," June 1979.)

randum detailed the Company's financial history as well as its debt structure with the Bank and suggested a consolidation of all debt with a line of credit to keep Hanson "in business". To prevent the use of money from the line of credit to make payments on term debt (much like using a credit card to pay a car payment), Gurbach suggested that withdrawals be restricted based upon construction progress. Additionally, Gurbach stated that when cash flow was poor during the winter months, Hanson would have to fund operations from his own assets.

On July 12, 1985, Hanson met with Bank officers to discuss the restructure of the Company debt. In that meeting, the head of American National's Corporate Service Department, Willie McElroy, insisted that if the Bank was to re-write the debt, Hanson would have to secure it with a second mortgage on his home. Although purchased with marital funds, the home was titled in only Virginia Hanson's name.

On July 15, 1985, Hanson wrote the Bank a letter that set out his "proposal for the loan committee's consideration." It proposed a $125,000.00 operational line of credit "for the continued operation of the Company" to be secured only by receivables. It mentioned no other financing for future operations.

However, according to Hanson, he later contacted David Chesnut, Executive Vice President of the Bank and his former loan officer. Hanson said that Chesnut told him that if he granted a second mortgage to secure Company debt, the Bank would restructure the debt on a three (3) year balloon note, renewable for up to fifteen (15) years, and that the Bank would finance all of his future contracts for up to fifteen (15) years in an amount equal to twenty

percent (20%) of the contract at the Bank's then prevailing interest rate.

A closing of the restructured debt occurred on July 26, 1985. McElroy was on vacation and not present. The restructured debt was closed by another Corporate Service Officer and the Bank's counsel. The closing documents consisted of the restructure note, which consolidated six of the outstanding notes of Hanson Construction (the $125,000 line of credit was left open), a seven page loan agreement that summarized the entire transaction, and various mortgages and security agreements.[2] The closing lasted approximately an hour and forty-five minutes.

Hanson admitted that he signed the documents even though he did not read them. According to Hanson, the closing attorney objected to him reading the documents, saying it would take all day. Hanson said the loan documents he signed did not reflect Chestnut's alleged promises and that the Bank dissuaded him from reading the documents as part of a fraudulent scheme to obtain additional collateral (the "Fraudulent Inducement Claim").

In January 1987, Hanson approached McElroy for additional funding on a new contract that he was negotiating. He also requested an interest reduction on his debt to the Bank. Hanson's requests were reviewed by the Executive Loan Committee. The Committee noted that the cash

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[2] Significant differences existed between the Gurbach Memorandum and the restructure actually effected. Hanson Construction was granted operating funds during the winter. The restructure note of July 26, 1985 did not require debt service during the winter months. The $125,000.00 operating line of credit was not restricted.

flow from operations was insufficient to service debt[3], that the Company was unable to obtain bonding, was highly leveraged, and its equipment was aging. On February 5, 1987, the Committee denied Hanson's requests and prohibited future draws on the existing lines of credit, except that the Bank permitted three weeks of additional draws for the Company to meet payrolls while it sought financing elsewhere.

On March 11, 1987, American National called two demand notes, representing the Company's operational line of credit and another line established in 1986 for a specific contract. The restructure note was not called. The Company defaulted on the March payment. The Hansons sued the Bank on April 13, 1987.

In its amended pleadings, the Bank raised the defense that the imposition of punitive damages in this matter would violate its constitutional rights to due process.

At trial, Hanson introduced proof to recover under the following theories in addition to the Fraudulent Inducement Claim: breach of the duty of good faith, breach of oral contract, breach of fiduciary duty, intentional infliction of extreme emotional distress, and physical injury. At the close of the Hansons' proof, and again at the close of all of the proof, the Bank moved for directed verdicts. The court dismissed the Hanson claims based upon breach of oral contract, breach of fiduciary duty, intentional infliction of extreme emotional distress, and physical injury. The Bank

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[3] The Company's 1986 audit showed a paper profit of $3,515.00. Hanson's auditor admitted that a payment to an affiliated company, on Hanson's books as a loan rather than a payment, and the double-booking of inventory, accounted for an approximate $100,000.00 "swing" in the last month of the year.

requested that the court instruct the jury of its decisions, arguing that the jury had heard the proof related to those claims and that such an instruction was necessary for the jury to be properly instructed. The court refused.

On January 25, 1989, the jury returned its verdict against American National on the Fraudulent Inducement Claim. The Hansons were awarded compensatory damages in the sum of $1,065,000.00 and punitive damages in the sum of $5,775,000.00. A judgment was entered on January 27, 1989.

On February 6, 1989, American National filed a motion for a new trial, for judgment notwithstanding the verdict, and/or remittitur. In those motions, it again raised the constitutional issue of due process. At a hearing on those motions, the trial court stated, in effect, that it had *no discretion* to review the amount of punitive damages.

American National appealed the trial court's amended judgment to the Kentucky Court of Appeals. American National again raised the constitutionality of the imposition of punitive damages before that court. Recognizing the review standards approved in *Haslip*, the Kentucky Court of Appeals attempted to reconcile those standards with existing Kentucky law. The Court of Appeals affirmed the finding of fraud. However, it determined that punitive damages were excessive and reversed that portion of the amended judgment and remanded for either a new trial and/or remittitur.

Both parties sought and were granted discretionary review before the Supreme Court of Kentucky. American National again raised the constitutionality of the imposition of punitive damages under the facts of the case. After finding that the instructions given to the jury met the

Haslip standards, the Kentucky Supreme Court simply noted that post-trial review also "conformed to the test." It then reiterated the existing law in Kentucky which is based upon excessiveness, denominated the "first blush" rule. Thus, the Kentucky Supreme Court noted the *Haslip* standards, but failed to apply them. It erroneously held that the most cursory post-trial review, the "first blush" rule, is the equivalent of the standards approved by this Court in *Haslip*.

REASONS FOR GRANTING THE WRIT

I. THE KENTUCKY SUPREME COURT ESTABLISHED PROCEDURAL STANDARDS FOR THE IMPOSITION AND REVIEW OF PUNITIVE DAMAGE AWARDS THAT DENY PROCEDURAL DUE PROCESS.

It is beyond question that rights guaranteed by the Fourteenth Amendment to the Constitution of the United States apply to proceedings in civil actions tried in state courts. *Sniadach* v. *Family Fin. Corp*, 395 U.S. 337 (1969); *Fuentes* v. *Shevin*, 407 U.S. 67, (1972); *North Georgia Finishing, Inc.* v. *Di-Chem, Inc.*, 419 U.S. 601 (1975); *Connecticut* v. *Doehr*, __ U.S. __, 111 S.Ct. 2105 (1991). Property rights have been considered by this Court to be basic civil rights. *Lynch* v. *Household Fin. Corp.*, 405 U.S. 538, (1972). The application of federal constitutional standards in determining the appropriateness of punitive damages has received much attention in recent decisions of this Court. See *Gertz* v. *Robert Welch, Inc.*, 418 U.S. 323 (1974); *Bankers Life & Casualty Co.* v. *Crenshaw*, 486 U.S. 71 (1988); and *Browning-Ferris Indus. of Vermont, Inc.* v. *Kelco Disposal, Inc.*, 492 U.S. 257 (1989).

In *Pacific Mut. Life Ins. Co.* v. *Haslip*, 499 U.S. __, 111 S.Ct. 1032 (1991), this Court discussed at length the pa-

rameters of punitive damages within the confines of the due process clause of the United States Constitution. While this Court upheld the imposition of punitive damages in that case, it stated that ". . . general concerns of reasonableness and adequate guidance from the court when the case is tried to a jury properly enter into the constitutional calculus." *Haslip*, 111 S.Ct. at 1043. This Court then discussed constitutionally acceptable standards in three phases of the litigation process: instructions to the jury, post-trial review by the trial judge, and appellate review. American National has been denied constitutionally acceptable standards in all three phases and, thus, its constitutional rights to due process under the Fourteenth Amendment.

The appellate courts of other states have recognized *Haslip* as constitutional direction regarding their award of punitive damages. The Supreme Court of Appeals of West Virginia in *Garnes* v. *Fleming Landfill, Inc.*, 413 S.E.2d 897 (W.Va. 1991), acknowledged that *Haslip* mandated a restructure of that state's appellate review process with respect to punitive damage awards. It noted:

> We believe that the U.S. Supreme Court's adoption of punitive damages standards is a major step in the unification of America's decisional law in matters where the separate states are unable to craft a set of rational rules. State courts have adopted standards that are, for the most part, not predictable, not consistent, and not uniform. Such fuzzy standards inevitably are most likely to be applied arbitrarily against out-of-state defendants.[4]

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[4] While American National was located in Bowling Green, Kentucky, Hanson's counsel, in closing, asked the jury, in awarding punitive damages, to send a message to Louisville and Cleveland (the cities where the Bank's holding companies are located); he sought exactly the type of arbitrary action the West Virginia court suggested fuzzy standards fostered.

Id. at 905 (citations omitted). Other states applying the *Haslip* standards include Maryland, New Jersey, and Tennessee.[5] *See* Sup. Ct. R. 10.1(b).

Moreover, since this Court's decision in *Haslip*, it has granted review of a number of cases from either the highest court of the respective state, or the United States Circuit Court of Appeals, applying state law in cases in which punitive damages were imposed. This Court has, consistent with *Haslip*, granted review and reversed in at least eleven cases.[6]

A. The Jury Instructions Were Insufficient To Prevent The Jury From Considering Extraneous, Inflammatory, And Legally Insufficient Claims.

In discussing the instructions in *Haslip*, this Court noted that those instructions accommodated Pacific Mutual's interest in rational decision making and the state's interest

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[5] A partial list includes: *Alexander & Alexander, Inc.* v. *B. Dixon Evander & Assoc., Inc.*, 596 A.2d 687 (Md. Ct. Spec. App. 1991), *cert. denied*, 605 A.2d 137 (Md. 1992); *Herman* v. *Sunshine Chem. Specialties, Inc.*, 608 A.2d 978 (N.J. Super. Ct. App. Div.), *cert. granted*, 614 A.2d 620 (N.J. 1992); *Hodges* v. *S.C. Toof & Co.*, 833 S.W.2d 896 (Tenn. 1992).

[6] *Fleming Landfill, Inc.* v. *Garnes*, 499 U.S. __, 111 S.Ct. 2882 (1991); *Portec, Inc.* v. *The Post Office*, 499 U.S. __, 111 S.Ct. 1299 (1991); *Pacific Lighting Corp.* v. *MGW, Inc.*, 499 U.S. __, 111 S.Ct. 1299 (1991); *International Society for Krishna Consciousness of California* v. *George*, 499 U.S. __, 111 S. Ct. 1299 (1991); *Church of Scientology of California* v. *Wollersheim*, 499 U.S. __, 111 S.Ct. 1298 (1991); *Hospital Authority of Gwinnett County* v. *Jones*, 499 U.S. __, 111 S. Ct. 1298 (1991); *Reserve Life Ins. Co.* v. *Eichenseer*, 499 U.S. __, 111 S.Ct. 1298 (1991); *Clayton Brokerage Co. of St. Louis, Inc.* v. *Jordan*, 499 U.S. __, 111 S.Ct. 1298 (1991); *Intercontinental Life Ins. Co.* v. *Lindblom*, 499 U.S. __, 111 S.Ct. 1575 (1991); *AMCA Int'l Fin. Co.* v. *Hilgedick*, 499 U.S. __, 111 S.Ct. 1614 (1991); *Transamerica Occidental Life Ins. Co.* v. *Koire*, 499 U.S. __, 111 S.Ct. 2253 (1991).

in the assessment of appropriate deterrence and retribution. Thus, both the defendant and the state had an interest to be protected. Neither of those interests were met in this case through the instructions given to the jury.

American National was denied its right to a trial by jury properly instructed. The Bank did not object at trial and does not raise here the question of whether the punitive damage instruction actually given to the jury was correct. That instruction was a correct and accurate representation of Kentucky's punitive damage statute, KY. REV. STAT. ANN. §411.186 (Michie 1992). However, the test should not end there. The jury instructions *in toto* did not meet American National's constitutional right to due process, because the jury was not instructed that the court had directed verdicts on a number of the theories and issues, the theories most likely to incite passion and prejudice on the part of the jury and about which they had heard evidence.

Hanson testified that after the Bank denied his Company credit, he considered suicide as an option. His alleged thought process was that insurance proceeds would satisfy the debt and save his good name. The trial court held, as a matter of law, that Hanson failed to prove intentional infliction of extreme emotional distress. However, the court refused to instruct the jury of that decision or to otherwise limit the effect of that testimony.

Hanson was permitted to testify that because the Bank called his loans he became a common laborer for his son's company. In that capacity, he was forced to move a heavy battery. As a consequence, he suffered a back injury. While the trial court ruled that injury had an insufficient nexus with the actions of the Bank, it refused to advise the jury of its decision or to admonish them to not consider testimony about physical injury and pain.

Additionally, Hanson testified that he had over the years developed a relationship of trust with the Bank. The context of that testimony was not to establish reliance for the purpose of fraud but rather to prove that the Bank was the fiduciary of Hanson. The trial court rejected Hanson's argument that the Bank was his fiduciary but also refused to instruct the jury of that decision.

During the trial, Hanson offered significant testimony regarding the alleged oral contract he had made with the Bank. He testified that the Bank had committed to renew his July 26, 1985 note for up to fifteen (15) years. Moreover, he testified that the Bank had committed to fund all future contracts he obtained—without regard to legal lending limits or other federal constraints—in an amount up to twenty percent (20%) of the contract at the Bank's then prevailing interest rate. The Bank was granted a directed verdict on that theory. The Bank sought to have the jury instructed as to that matter, but the trial court refused.

The jury was not properly instructed because it was not instructed as to the directed verdicts on the claims through which irrelevant and inflammatory evidence was introduced. The Petitioner recognizes that Kentucky has long followed the "bare bones" test for instructions. But in a case where the plaintiff demands not just compensatory damages relating to specific instructions, but additionally demands a much larger sum of punitive damages, a state's long recognition of a particular form of instructions does not, necessarily, meet the standards of constitutional protection. The jury should have been instructed to disregard the irrelevant and inflammatory evidence in its deliberation on the award of punitive damages.

Other states have recognized that a jury cannot be properly instructed unless it is told what has been removed from its consideration. In *Missouri Highway & Transp. Comm'n* v. *Wallach*, 826 S.W.2d 901 (Mo. Ct. App. 1992), the Missouri Court of Appeals stated: "A withdrawal instruction is appropriate where the jury might infer from the evidence presented that inappropriate factors relating to damages were included." *Id.* at 903.

Arizona and Indiana have recognized the same right. *Young* v. *Environmental Air Prod., Inc.*, 665 P. 2d 88 (Ariz. 1982); *Park County* v. *Roepack, Inc.*, 526 N.E.2d 732 (Ind. Ct. App. 1988). But the Hanson jury, which heard testimony about a contemplated suicide and physical injury, and which imposed an award of punitive damages in excess of five times the compensatory award, was not so instructed. By failing to so instruct the jury, the trial court denied American National its right to due process.

B. The Duties Of A Kentucky Trial Court In The Review Of Punitive Damage Awards, As Understood By Both The Trial Judge And The Kentucky Supreme Court, Are Inconsistent With Due Process.

In *Haslip*, this Court severely questioned the review of punitive damage awards by state courts under the meager and imprecise test of whether the award "evinces passion, bias and prejudice." *Haslip*, 111 S.Ct. at 1045 n.10. The Court noted that it had "expressed concern" in *Browning-Ferris*, 492 U.S. 257 and *Bankers Life*, 486 U.S. 71, about this type of limited trial court review. Yet, that is precisely the standard applied in this case.

In contrast, the *Haslip* Court cited with approval Alabama's much more comprehensive post-trial review.

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Among the factors on which this Court focused was the presence of a "meaningful and adequate review *by the trial court* whenever a jury has fixed the punitive damages." *Haslip*, 111 S.Ct. at 1044 (emphasis added). This Court noted that an Alabama trial judge will "reflect in the record the reasons for interfering with a jury verdict, or refusing to do so, on grounds of excessiveness of the damages." *Id.* (quoting *Hammond* v. *City of Gadsden*, 493 So.2d 1374, 1379 (Ala. 1986)). Furthermore, the Alabama trial court was expected to consider the following:

1. the culpability of the defendant's conduct;
2. desirability of discouraging others from similar conduct;
3. impact upon the parties; and
4. other factors such as the impact on innocent third parties.

The inaction of the Kentucky trial court and the decision of the Kentucky Supreme Court flout this Court's emphasis and direction with respect to trial court review.

Specifically, while recognizing some problems with the punitive damages award, the trial court provided the following explanation as to why it could not act to protect American National:

> Usually a judgment of this nature causes all of us to pause and think about not only the case, but throughout this system as a whole and how it should function, whether it functions properly. The function of a trial judge is a little different from the function of an appellate judge. I can't—there are times when I have to decide issues that have not been decided before, and to do that, I try to look at decisions from other jurisdictions to see if they're logical, and if they make sense, and then I just have to rely on my own experience and training and instincts to make decisions.

> In other instances, there are decisions of the Supreme Court and the Court of Appeals which are binding upon me, and when there are, I must follow those decisions. I don't really have any choice. . . . I'm concerned, and I've expressed this concern during the trial, that punitive damages have a very important function in our law, and I think they serve a useful purpose. I'm concerned that in some instances, the punitive damages may have gotten out of hand to the point where they don't serve the function of merely punishing, but they serve the function of destroying.
>
> However, our Supreme Court has taken the view, as I've indicated, even as recently as this year or late last year, that it would not disturb a—and the Court of Appeals took a similar view—that it would not disturb a verdict out of this court involving punitive damages over 42 times the compensatory damages; so they apparently do not consider that in arriving at a decision.[7]

Thus, the trial court exercised no discretion, because it believed it had none. This standard of review applied to American National is plainly insufficient under *Haslip* where this Court stated that state court procedures must impose "a sufficiently definite and meaningful constraint on the discretion of . . . fact finders in awarding punitive damages." *Haslip*, 111 S.Ct. at 1045.

Unfortunately, the Kentucky Supreme Court's opinion on the power of a trial court to interfere with a punitive

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[7] This statement was made, on the record, by the trial judge at a hearing on the Bank's motion for new trial, judgment notwithstanding the verdict, and/or remittitur. In that motion, the Bank argued *inter alia*, that the punitive damages award was excessive, that the jury was inflamed by the evidence related to theories on which directed verdicts had been granted but no withdrawal instructions given, and that the imposition of the damages violated its constitutional rights. The Kentucky Court of Appeals recognized in its decision the trial court's focus on the 42 multiple of compensatory damages. (App., p. 31a).

damages award is equally deficient. Citing *Davis* v. *Graviss*, 672 S.W.2d 928 (Ky. 1984), the Kentucky Supreme Court stated that it was sufficient for a trial court to apply what is known in Kentucky as the "first blush" rule.

In *Davis* v. *Graviss*, the "first blush" rule was explained as follows:

> The 'first blush' rule is a mechanism to assist the *trial court* in performing its responsibility when called upon to decide whether the award is so excessive as to appear 'to have been given under the influence of passion or prejudice.' C.R. 59.01(d). In its entirety it is that 'a verdict may be set aside as excessive only if 'it is (so) to such an extent as to cause the mind at first blush to conclude that it was returned under the influence of passion or prejudice on the part of the jury.'

Id. at 932 (court's emphasis).

Interestingly, the *Davis* case did not even involve a punitive damage award. There, the plaintiff sustained substantial physical injuries in an automobile accident and was awarded solely compensatory damages in the amount of $309,000.00.[8]

Whatever the merits of a "first blush" test may be for reviewing compensatory damages for personal injury claims, the *Haslip* Court's contrasting of the Alabama procedure with that of Vermont and Mississippi indicates that it is wholly inappropriate in the context of a punitive damages award. *Haslip*, 111 S.Ct. at 1045 n.10.

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[8] Ms. Davis' injuries included a broken nose, dislodged teeth, dizziness, a concussion, and a basilar skull fracture which caused a leakage of spinal fluid creating a danger for future meningitis, brain abscesses and other neurological problems. *Davis*, 672 S.W.2d at 929.

C. There Is No Meaningful Appellate Review Of Punitive Damage Awards In Kentucky As The Appellate Court Can Only Reverse If It Finds The Trial Court Abused Its Discretion As To The Factual Existence Of Passion Or Prejudice By The Jury.

The Kentucky Supreme Court compounded its error with respect to the trial court's review authority by establishing that the proper standard for appellate review is whether the trial court abused its discretion in making the factual determination of bias and prejudice on the part of the jury. This standard stands in stark contrast to that approved in *Haslip*.

In *Haslip*, this Court noted that Pacific Mutual had "received the benefit of *appropriate* review by the Supreme Court of Alabama." *Id.* at 1046. (emphasis added). This Court approved the following criteria for use by appellate courts in the review of punitive damage awards:

a) whether there is a reasonable relationship between the punitive damage award and the harm likely to result from the defendant's conduct as well as the actual harm;

b) the degree of reprehensibility of the defendant's conduct, its duration, the defendant's awareness, any concealment, and the existence and frequency of similar past conduct;

c) the profitability of the wrongful conduct;

d) the financial position of the defendant;

e) the cost of litigation;

f) the imposition of criminal sanctions; and

g) the existence of other civil awards.

Id. at 1045.

Use of these criteria permitted a determination of "whether a punitive award is reasonably related to the goals of deterrence and retribution." *Id.* The *Haslip* deci-

sion further noted that Alabama had actually applied these criteria to reduce punitive damage awards.

In contrast to the strict *de novo* review used by Alabama appellate courts, the rule established for Kentucky is only whether the trial court abused its discretion in applying the "first blush" test. In *Davis* (the authority relied upon by the Kentucky Supreme Court in this case), the court noted that "the appellate function [for reviewing jury damage awards] is properly described in *Prater* v. *Arnett* . . .", *Davis*, 672 S.W.2d at 932. The court then went on to quote the following passage in *Prater*:

> Upon reviewing the action of a trial judge in (granting or denying a new trial for excessiveness), the appellate court no longer steps into the shoes of the trial court to inspect the actions of the jury from his perspective. Now, the appellate court reviews only the actions of the trial judge . . . to determine if his actions constituted an error of law. There is no error of law unless the trial judge is said to have abused his discretion and thereby rendered his decision clearly erroneous. Further, the action of the trial judge is presumptively correct . . . .

Id. (*quoting Prater* v. *Arnett*, 648 S.W.2d 82, 86 (Ky.Ct.App. 1983)).

Haslip's focus on careful application of punishment through punitive damages reflects fundamental aspects of due process. Even wrongdoers are granted "protection of the individual against arbitrary action of the government." *Daniels* v. *Williams*, 474 U.S. 327, 331 (1986) (quoting *Dent* v. *West Virginia*, 129 U.S. 114 (1889)). Yet there is no possibility of determining what is or is not "arbitrary" unless state appellate courts examine the appropriateness of the punitive award by using more than the platitude of "first blush."

While paying lip service to this Court's opinion in *Haslip*, the Supreme Court of Kentucky reiterated and restated that "gentle rule" of excessiveness:

> It is with equal caution that this Court does not substitute its opinion as to the amount of exemplary damages for that of the jury. It was the trial jury and trial judge who heard all the evidence and had the opportunity to see and hear the witnesses during the lengthy trial. The sanctity of the jury verdict is at the heart of our judicial system.

(App., p. 14a). Thus, the Kentucky Supreme Court denied American National its constitutional right to meaningful review.

Had the Supreme Court of Kentucky applied even some of the standards approved in *Haslip*, it would have had to consider:

a) *The Bank Could Not Have Reasonably Anticipated Damaging The Hansons By Over A Million Dollars.* The Court would have had to consider whether or not a bank could have forseen such losses when Hanson Construction had experienced years of operating losses, had a negative net worth of [$168,224.00] as of the date of the cut-off of credit, and was in the highly speculative heavy construction industry.[9]

b) *The Likely Gain To The Bank Was Minimal.* The Court would have had to consider the gain the Bank was receiving by fraudulently inducing the Hansons to provide additional collateral when the Bank, in any event, could have obtained a judgment lien on the Hansons' property in excess of

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[9] Missouri has denied the award of lost profits in the heavy construction industry, holding, as a matter of law, such damages to be highly speculative. *Riddle* v. *Dean Mach. Co.*, 564 S.W.2d 238 (Mo. Ct. App. 1978).

the equity of the Hansons' in that collateral (subject only to the minimal Kentucky exemptions).[10]

The Kentucky Court of Appeals recognized the need for a more detailed review of a punitive damage award. The Court of Appeals considered that punitive damages "should be measured by the injury inflicted and its cause" and that "the injury inflicted and its cause" should be taken into account. The Court of Appeals also considered whether the injury inflicted was "substantial" and whether the actor tried "to remedy its misconduct". The absence of a serious danger of physical injury and the deterrent effect of the $1.065 million dollar compensatory award were also mentioned. After considering all of these factors, the Court of Appeals decided that punitive damages of more than three times compensatory damages was excessive in this case. (App., pp. 32a-33a).

The substitution by the Kentucky Supreme Court of a "first blush" test for the Court of Appeals' efforts to provide a serious analysis consistent with due process was reversible error.[11]

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[10] The Hansons argued that the Bank's fraud was designed to obtain a second mortgage on the home titled in Virginia Hanson's name. However, prior to the restructure, she was already personally obligated for $300,000.00 of Company debt, a sum in excess of her net equity in the home. Thus, obtaining a second mortgage permitted the Bank to benefit only to the minimal extent of eliminating Kentucky's $5,000.00 homestead exemption. KY. REV. STAT. ANN. §427.060.

[11] It is American National's position that the review standards applied by the Kentucky Court of Appeals, although similar to the standards approved in *Haslip*, fell far short of the standards required to provide due process. The authority for the "first blush" rule is cited, the trial court's responsibility to conduct a thorough review is not clearly stated, and the need for *de novo* appellate review is not established.

II. AMERICAN NATIONAL WAS DENIED ITS FOURTEENTH AMENDMENT RIGHT TO SUBSTANTIVE DUE PROCESS.

In *Browning-Ferris*, 492 U.S. 257, this Court noted that authority existed to place an outer limit on damages awarded pursuant to a statutory scheme (presumably such as the punitive damage statute codified at KY. REV. STAT. ANN. §§411.184 and 411.186) but that it had never addressed the precise question as to whether substantive due process acted as a check on undue jury discretion in awarding punitive damages. This Court suggested that that inquiry awaited another day.

Then in *Haslip*, before this Court began its analysis of procedural due process, it suggested that unlimited discretion in fixing punitive damages could jar "constitutional sensibility" *Haslip*, 111 S.Ct. at p. 1043. In a case such as this, where the only injury is financial, and in which compensatory damages are clearly adequate, the award of punitive damages in excess of five times the compensatory damages, and in an amount equal to one-half of the net worth of the defendant, jars those sensibilities.

The Kentucky Court of Appeals, without stating its concerns in constitutional terms, recognized the problem. The court noted that the only damages to Hanson were financial and that the award of compensatory damages was adequate. It referenced the various statutory schemes under which damages are multiplied. Having engaged in that analysis, it determined that the punitive damages awarded were excessive and reversed them for either a new trial or remittitur, with a cap for this case stated as a multiple of three times the compensatory damages. Thus, as a matter of policy or substantive due process, the Ken-

tucky Court of Appeals tried, for this case, to draw the "mathematical bright line" described as difficult in *Haslip*.

The Kentucky Supreme Court reversed that part of the decision of the Kentucky Court of Appeals, holding in essence that jury discretion was limited only by the "gentle rule" of excessiveness impliedly criticized by this Court in *Gertz*, 418 U.S. at 418. Such a standard did not and cannot protect American National's rights to substantive due process.

This case, like many modern cases, demonstrates the evolution of the "contort". "Contort" cases attempt to recover under a number of theories where the underlying relationship is contractual. California and Montana were quick to permit recovery of punitive damages for the tort of bad faith, one of the claims made by Hanson. *Seaman's Direct Buying Ser., Inc.* v. *Standard Oil Co.*, 686 P.2d 1158 (Cal. 1984); *Nicholson* v. *United Pacific Ins. Co.*, 710 P.2d 1342 (Mont. 1985). However, both California and Montana have recognized the dangers implicit in this approach. *Story* v. *City of Bozeman*, 791 P.2d 767 (Mont. 1990) addressed the problem:

> Parties have traditionally been free to breach their contract and pay contract damages whenever performance was not economically efficient. The relatively simple calculation of whether it is more profitable to breach a contract and pay damages rather than to perform is now complicated by the possibility of more indefinite tort damages.... This problem, however does not support tort damages.

Id. at 774.

Other states have used substantive due process as the basis to reduce punitive damage awards. In *Alexander & Alexander, Inc.* v. *B. Dixon Evander & Assoc., Inc.*, 596 A.2d 687 (Md. Ct. Spec. App. 1991), *cert. denied*, 605 A.2d

137 (Md. 1992), a Maryland Court of Appeals noted that nothing had been done to endanger the public health and safety, and that the defendant's conduct had not been life threatening. It then reversed the award of punitive damages stating:

> If faced with a punitive award that was entered upon proper procedure but which nonetheless contravenes due process because it is out of all proportion to both the harm caused and the perniciousness of the conduct, we could not, on the ground of judicial impotence, allow the unconstitutional award to stand.

Id. at 710. Those same considerations should have been applied in this matter.

While a "mathematical bright line" may be difficult to draw, a reasonable line should be drawn. In her dissent in *Haslip*, Justice O'Connor noted the explosion of punitive damages. She correctly attributed much of it to the type of changes discussed by the Supreme Court of Montana in *Story*, 791 P.2d 767. This Court should recognize that constitutional constraints exist on the size of an award of punitive damages and so hold in this case.

The common law, from which punitive damages have evolved suggests at least two criteria by which the size of an award of punitive damages may be measured. First, the award of punitive damages must bear some rational relationship to the injury suffered. Secondly, the award of punitive damages must meet the state's interest in deterrence while at the same time, not destroy the defendant. When the award of punitive damages in this case is measured against these criteria, it is excessive.

A. Punitive Damages Must Bear A Relationship To The Injury.

Under Kentucky law the amount of punitive damages must bear a reasonable relationship to the injury caused.

Louisville & N.R. Co. v. *Roth*, 114 S.W. 264 (Ky. 1908). The injury to Hanson was the destruction of the Company. The injury inflicted was financial. There was no personal injury, loss of life, or a danger of either. This led the Kentucky Court of Appeals to say:

> The award of compensatory damages was substantial and would seem to have more than slight deterrent effect on future deceptive conduct by the Bank. Comparing the amount of punitive damages assessed with the injury sustained and the fraud which caused it, and taking into account the relevant statutory factors, we believe that the award made by the jury was so disproportionate that the trial court should have interfered.

(App., p. 32a). Thus, the Kentucky Court of Appeals engaged in what was, in essence, a partial *Haslip* review and determined that given the relevant statutory factors, and the nature of the injury, that the punitive damages were excessive. It was that analysis which the Supreme Court of Kentucky reversed, and by so doing, deprived American National of its constitutional due process.

When the trial court engaged in its post-trial analysis, it reviewed the punitive damage award only as a numerical factor of the compensatory damages. In so doing, it compared those damages to cases decided by the Supreme Court of Kentucky involving physical injury. The trial court and the Supreme Court of Kentucky compared apples to oranges. There was no physical injury cognizable in this matter.

However, the most reasonable explanation of the amount of the punitive damage award in this case is that the Bank was denied its procedural rights to due process. Testimony regarding psychological and physical injuries was presented to the jury and it was not instructed to

disregard them. Procedural errors such as these clearly caused the punitive damage award to exceed any rational relationship to the actual injury. By affirming these damages, the Kentucky Supreme Court permitted American National's rights to substantive due process to be violated.

B. Punitive Damages Must Not Destroy The Defendant.

Additionally, the common law and Kentucky courts have recognized the interest of the state in punishment and deterrence. In *Bisset* v. *Goss*, 481 S.W.2d 71 (Ky. 1972), the former court of appeals, now Supreme Court of Kentucky, quoting from 25 C.J.S. *Damages* §117(1) (1966), noted:

> According to the more generally accepted doctrine, such damages are allowed not because of any special merit in the injured party's case, but are awarded by way of punishment to the offender, and as a deterrent, warning, or example to the defendant and others, or even, it has been said as an expression of the indignation of the jury.

Bisset, 481 S.W.2d at 74. This Court approved punishment and deterrence as a part of the state's rational decision making. *Haslip*, 111 S.Ct. at 1044. Concepts of punishment and deterrence, however, are not without limitation. The principle limitation imposed by the common law on punishment is that it may not destroy the defendant.

The United States Court of Appeals for the Second Circuit faced solely and squarely the question of excessive punitive damages in *Vasbinder* v. *Scott*, 976 F.2d 118 (2nd Cir. 1992). The action was brought by a former employee against an employer under 42 U.S.C.A.§1983 (West 1981). Liability had been determined in a previous trial and ap-

peal. In the subsequent trial, the employee was awarded punitive damages of $150,000.00. In its review, the Second Circuit stated:

> Accordingly, an award should not be so high as to result in the financial ruin of the defendant (citation omitted). Nor should it constitute a disproportionately large percentage of a defendant's net worth. Thus, while a defendant's conduct is obviously germane to the damages issue, 'even outrageous conduct will not support an oppressive or patently excessive award of damages' (citations omitted). Further, because neither compensation nor enrichment is a valid purpose of punitive damages, an award should not be so large as to constitute 'a windfall to the individual litigant' (citations omitted). Finally, in applying these principles, we must engage in an independent and 'detailed appraisal of the evidence bearing on damages' (citation omitted).

Id. at 121.

In *Herman* v. *Sunshine Chem. Specialties, Inc.*, 608 A.2d 978 (N.J.Super. Ct. App. Div.), *cert. granted*, 614 A.2d 620 (N.J. 1992), the Superior Court of New Jersey reviewed an award of punitive damages in a negligence action. The court recognized that the evidence of the financial condition of the defendant was a necessary factor for review because it "must be reviewed by an appellate court to determine if it 'exceeds the level necessary to properly punish and deter. . . .'" *Id.* at 985 (quoting *Adams* v. *Murakam*, 54 Cal. 3d 105, 813 P.2d 1348, 1350, 284 Cal. Rptr. 318 (1991)).

The decision of the Supreme Court of Kentucky in this matter presents an anomaly in Kentucky law. Under prior case law, in actions for punitive damages, the parties were not permitted to present evidence of the financial condition of either side of the litigation. *Hensley* v. *Paul Miller*

Ford, Inc., 508 S.W.2d 759 (Ky. 1974). However, in 1988, the Kentucky legislature enacted KY. REV. STAT. ANN. §§ 411.184 and 411.186 in an attempt to reduce awards of punitive damages. The "profitability of the misconduct of the defendant" is one of the criteria to be evaluated. KY. REV. STAT. ANN. §411.186(c). In its review of the punitive damages, the Supreme Court of Kentucky ignored this Court's guidance in *Haslip*, and the Kentucky legislature's statutory guidelines.

Hanson presented to the jury the financial condition of American National. Hanson's evidence established that in the year of his alleged wrong, American National lost [$743,000.00]. The balance sheet revealed to the jury showed that the total equity of the Bank was $11,897,000.00. The jury awarded Hanson $5,775,000.00 in punitive damages. That award represented 48½% of the total equity of the Bank.

Absent the intervention of the holding company, it would have reduced the capital of the Bank to $6,122,000.00 giving it a capital to assets ratio of 3.3%, well below regulatory standards for national banks. Without the financial support and strength of the Bank's holding company, its very existence as a viable entity would have been jeopardized by this award of punitive damages. The Supreme Court of Kentucky refused to consider this fact[12]. Its refusal denied American National substantive due process.

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[12]In a "lender liability" case similar to this case (allegations of fraudulent misrepresentation in regard to future financing), the Supreme Court of Mississippi, in reversing a judgment against a bank, took judicial notice that a bank occupies the unique position of simultaneously being a "public institution and a private investment." *Bank of Shaw* v. *Posey*, 573 So.2d 1355, 1363 (Miss. 1990).

CONCLUSION

When confronted with this Court's opinion in *Haslip*, other states have modified their standards and procedures to afford defendants constitutional due process rights with respect to the award of punitive damages. Kentucky, however, refuses to do so. While it paid only lip service to *Haslip*, it in reality reaffirmed the gentle rule of excessiveness, which this Court suggested in footnote 10 to *Haslip* was unacceptable.

This Court should review the decision of the Kentucky Supreme Court to insure that the *Haslip* standards for the due process review are carried out consistently, if not identically, by the various states. *See, Garnes*, 413 S.E.2d 897. If the decision of the Kentucky Supreme Court is not reviewed, the citizens of this Commonwealth will suffer the unconstitutional imposition of punitive damages by state action conditioned only upon the most cursory review by the trial courts, the "first blush" test. Kentucky citizens will not have the added protection of a review of fact criteria for the award by appellate courts. The citizens of Kentucky should enjoy a level of due process protection consistent with that of other states whose court's have correctly read the decision of this Court in *Haslip*.

This Court should grant the Bank's Petition for Certiorari and, upon review, vacate the judgment of punitive damages against the Bank.

Respectfully submitted,

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APPENDIX

RENDERED: December 17, 1992
TO BE PUBLISHED

SUPREME COURT OF KENTUCKY

91-SC-375-DG

H. C. HANSON, VIRGINIA HANSON,
H. C. HANSON CONSTRUCTION COMPANY, INC., and
CONSTRUCTION ENGINEERS, INC. - - - *Appellants*

Appeal From Court of Appeals
v. *Nos. 89-CA-000639 and 89-CA-000690*
(Warren Circuit Court No. 87-CI-318)

AMERICAN NATIONAL BANK & TRUST COMPANY - *Appellee*

AND

91-SC-377-DG

AMERICAN NATIONAL BANK & TRUST COMPANY - *Appellant*

Appeal From Court of Appeals
v. *Nos. 89-CA-000639 and 89-CA-000690*
(Warren Circuit Court No. 87-CI-318)

H. C. HANSON CONSTRUCTION COMPANY, INC.,
H. C. HANSON, VIRGINIA HANSON,
CONSTRUCTION ENGINEERS, INC., and
LUCILLE KINSLOW - - - - - - - - *Appellees*

OPINION OF THE COURT
BY SPECIAL JUSTICE PAUL L. MADDEN
REVERSING IN PART AND AFFIRMING IN PART

This is a consolidated appeal which raises several issues in the context of a lender liability claim. This Court has granted discretionary review of a decision of the Court of Appeals.

At the conclusion of a lengthy trial the jury returned a verdict finding the Defendant, American National Bank (hereafter referred to as Bank), had fraudulently induced the Plaintiffs, H. C. Hanson, his wife, Virginia Hanson, H. C. Hanson Construction Company, and Hanson Engineering, Inc., (hereafter referred to as Hanson), to restructure a loan on terms that the Bank had no intention of performing. The jury awarded Hanson compensatory and punitive damages.

The following statement of the facts of this case is not intended to be complete but is necessary for an understanding of the issues presented.

H. C. Hanson is the owner of Hanson Construction Company, Inc. and Hanson Engineering, Inc. These companies are engaged in the bridge construction industry. Hanson and the companies have been customers of the Bank since the 1970s and conducted most dealings with Mr. David Chestnut, a Bank officer.

During the early 1980s, Hanson began to experience financial difficulty and the Bank continued to finance the business. By 1985 Hanson had several notes at the Bank signed by Hanson personally and in his corporate capacity for the companies.

In 1985 American National Bank was acquired by First Kentucky National Corporation. In the same year a First Kentucky task force began a review of the customer accounts at American National to reclassify any substandard accounts. To avoid public reaction to the review process, customers, including Hanson, were not informed when their accounts were being reviewed and reclassified as substandard by the task force nor was Hanson advised that a memorandum had been prepared recommending that the Hanson debts be restructured and the line of credit be restricted. That interbank memo, dated July 8, 1985, rec-

ommended that the Bank obtain a second mortgage on the Hanson's home and farm, then titled to Virginia Hanson, to secure the restructured debts, to limit the line of credit, and to use a cut off of that credit to force Hanson to sell his personal holdings. The memo suggested that with the plan and by postponing foreclosure for several months the Bank would reduce its potential loss. This plan was refined and approved by the task force. Members of the task force met with Mr. Hanson to discuss the restructure. Hanson refused their plan. Mr. Hanson contacted Mr. Chestnut who explained the restructure plan given him. Mr. Hanson testified that Mr. Chestnut told him the Bank would finance up to 20% of new construction contracts to be rewritten annually until the jobs were completed. On July 15, 1985, Hanson drafted a letter in which he proposed a 15 year term on the restructured debt, a $125,000.00 line of credit and a $100,000.00 letter of credit secured by a second mortgage on the home and farm. The Bank informed Hanson that the entire debt must be secured by the second mortgage. Mr. Hanson testified that Chestnut notified him that with the second mortgage securing the full restructured debt, the Bank would give Hanson a $125,000.00 line of credit, provide financing for future contracts up to 20% of the contract amount and allow 15 years for repayment of the restructured loan.

The documents were prepared by the Bank's attorney and the restructured loan was closed on July 26, 1985. The closing document contained almost 100 pages. At the closing Mr. Hanson began to read the documents. The Bank's representative protested because of the length of time it would take and Hanson was assured that the documents contained all the understandings. Relying on this assurance, Mr. Hanson did not read the documents but did sign them. Contrary to Hanson's understanding, the closing documents did not contain terms for financing as allegedly represented by Mr. Chestnut.

In the spring of 1986, Mr. Hanson obtained contracts for two bridges and obtained a $175,000.00 line of credit from the Bank for this project. This debt is evidenced by a demand note dated June 1986. In October 1986, Hanson obtained a contract to build a bridge in Powell County but no financing by the Bank was requested at that time.

In January 1987, Hanson contacted the Bank for a loan on the Powell County project and on a bridge contract in Lewis County and for a reduction in interest. The Bank denied the request for funding in these two projects, denied the interest reduction and stopped additional draws on existing lines of credit. The Bank did agree to allow for draws of up to $21,000.00 to meet payroll and thereby allow time for Hanson to seek alternative financing. On March 11, 1987, the Bank demanded full payment of a 1984 note. The restructured note was called after Hanson missed the next scheduled payment.

Hanson filed the action in April 1987, alleging that the Bank's action in February and March 1987 forced Hanson Construction out of business. Hanson alleged breach of a fiduciary duty owed by the Bank, recision of the contract, and fraud and misrepresentation. The Bank counterclaimed for the debt owed it by Hanson. At the conclusion of the evidence the trial court entered a directed verdict for the Bank on the issue of breach of a fiduciary duty and recision of the contract. The trial court submitted to the jury only the issues of fraud and misrepresentation. The jury found for Hanson and awarded compensatory damages of $1,065,000.00 and punitive damages of $5,775,000.00. The trial court entered judgment on the verdict less amounts owed to the Bank by Hanson on the various notes, interest and legal fees. The Bank's motion for new trial and judgment NOV were heard by the trial court and denied.

The Court of Appeals affirmed the judgment of the trial court in all matters except the award of punitive damages.

The Court of Appeals reversed as to punitive damages and remanded the case to the trial court for remittitur of excessive punitive damages or the grant of a new trial on punitive damages. This Court has granted discretionary review to examine the claims of errors by the parties.

The decision and order of the Court of Appeals in remanding the matter to the trial court for remittitur of the excess of punitive damages or new trial on those damages is reversed. The decision of the Court of Appeals affirming the judgment in the award of compensatory damages is affirmed.

This is a tort action for compensatory and punitive damages for fraud and misrepresentation. This Court has held in *Kentucky Electric Development Co.'s Receiver* v. *Head*, Ky., 68 S.W.2d 1 (1934), where a fraud has been perpetrated to induce a party to enter into a contract, the injured party may elect to affirm the contract and recover damages in tort for the fraud or disaffirm the contract and recover the consideration with which he has parted. *Bryant* v. *Troutman*, Ky., 287 S.W.2d 918 (1956).

At the conclusion of the evidence Hanson chose the remedy to pursue. Since Hanson affirmed the contract, the trial judge directed a verdict on the contract documents for the Bank in the amount of the debts evidenced by the notes, interest and legal fees. The trial court submitted to the jury only the tort claim and instructed the jury accordingly, permitting the jury to assess damage, if any, for fraud.

The Bank argues that the trial court erred in not advising the jury of its directed verdicts against Hanson in the claims based on fiduciary duty and oral contract and claims for physical injury. The Bank contends that since the court did not instruct the jury of the directed verdicts, the jury was allowed to consider the evidence it heard of these claims in awarding the compensatory and punitive

damages. This Court cannot accept the argument. We find no authority to support that contention nor has any been cited to us. The Civil Rules, specifically CR 50.01, do not require that special instruction to the jury, and this Court is not prepared to hold that such an instruction should be given. It is within the discretion of the trial judge to determine whether that instruction should be given to the jury.

This case was submitted to the jury on interrogatories for special verdict thereby limiting the jury in its fact finding function. A special verdict in response to written questions made in accord with CR 49.01 best prevents the jury from considering immaterial issues and submits to the jury only the appropriate contested issues. *Robinson* v. *Murlin Phillips & MFA Insurance Company,* Ky., 557 S.W.2d 202 (1977). *Ford Motor Company* v. *Fulkerson,* Ky., 812 S.W.2d 119 (1991). The jury's verdict was returned on the issues submitted: whether the Bank made fraudulent misrepresentations to Hanson and Hanson justifiably relied upon such misrepresentations to their detriment.

The Bank argues that the representation or promises made by the Bank to Hanson were too indefinite to form the basis for a contract and therefore are unenforceable: Where the representations are not enforceable as contracts, as a matter of law, the representations cannot be the basis for an action for fraud. The essential element in an action for fraud is not whether the representation is the consideration for contract for which a separate action may lie.

> Since a promise necessarily carries with it the implied assertion of an intention to perform it follows that a promise made without such intention is fraudulent and actionable in deceit . . . This is true whether or not the promise is enforceable as a contract. *Restatement (Second) of Torts § 530* Comment c (1976).

The inducements presented by the Bank were specific: financing 20% of future projects, 15 year repayment of the restructured debt if paid as a agreed and a $125,000.00 line of credit. It was for the jury to decide if it was reasonable for Hanson to rely upon such inducements and whether Hanson in fact did rely.

The Bank contends that Hanson's failure to read the contract documents must, as a matter of law, bar any claim, including one based on fraud, which alleges facts or promises contradicted by the written contracts. Where the oral representations are contrary to the written language of the contract, recision of the written contract should not be permitted by the party who failed to read it. However, that party may yet have a cause of action based on fraud and deceit against the person who induced him to sign the contract. *Cline* v. *Allis-Chalmers Corporation,* Ky., 690 S.W.2d 764 (1985).

Where there is evidence that a party to a contract is induced to signing the contract without reading it, it is a question for the jury to determine whether that party exercised ordinary care under the circumstances in doing so. *Kreate* v. *Miller,* 11 S.W.2d 99 (1928).

If the jury determines that the party signing the contract without reading it exercised ordinary care and that the person who induced the party did so through fraud and misrepresentation, a tort action for fraud is the appropriate remedy.

Hanson presented evidence that he did not have an opportunity to read the contract, that he was discouraged from doing so, that the Bank had the documents several days before the closing and had not made these available to him for review, that he was discouraged from obtaining separate counsel to examine the documents and of the manner in which the Bank presented itself to obtain his confidence, all coupled with the assurances that the documents

were prepared as he and the Bank had agreed. In light of this evidence, it was properly left for the jury to determine whether Hanson exercised ordinary care of whether Hanson's failure to do so was so imprudent as to bar recovery for deceit.

The Bank argues that the loan documents must be enforced as written and any evidence to the contrary must be excluded under the parol evidence rule. It concludes that under this well-established rule that even though the evidence of the oral promise may prove fraud, all such evidence is inadmissible since it is at variance with the written document. The Bank would extend the parol evidence rule to include tort actions based on fraud and deceit. We do not accept its arguments. The rule announced in *Bryant* v. *Troutman*, Ky., 287 S.W.2d 918, 920 (1956), is accurately stated.

> The rule is that parol testimony is not admissible to vary the terms of a writing. When the negotiations are completed by the execution of the contract, the transaction, so far as it rests on the contract, is merged in the writing. But false and fraudulent representations made by one of the parties to induce the other to enter into the contract, are not merged in the contract. Parol evidence is admissible to show that the making of the contract was procured by fraudulent representations. This does not vary the terms of the contract.

The Bank claims that Hanson's action is based on an oral promise by the Bank to finance future projects and to renew the restructured note after three years to be paid over a period of 15 years; since that agreement could not have been performed within one year, any action on that oral agreement is barred by KRS 371.101. The Court of Appeals accurately defined the rule in this state that our statutes do not abrogate the common law remedy for fraud

merely because the fraudulent misrepresentation is not in writing. The rule has been unchanged since announced by this Court in *Vertrees* v. *Head & Matthews*, 127 S.W. 523, 524, 525 (1910).

> That part of the statute of frauds invoked to defeat a recovery has no application to the state of facts set out in the petition. If a person, in violation of law, or deceitfully or fraudulently, or with knowledge of its falsity, makes a representation or assurance concerning the character or credit of another, it is not essential to maintain a cause of action against him that such representation or assurance shall be in writing. The statute does not embrace assurances or representations that are deceitfully or fraudulently made, or that are made with knowledge of their falsity, or in violation of a statute. It was not intended to save harmless from consequences of false and fraudulent statements of wrongdoers, or those who for purposes of gain or other motive would cheat or mislead. It was designed to protect persons who honestly and in good faith made assurances respecting the credit or standing of another, and should be confined to this character of cases.

The Bank claims that inasmuch as Hanson continued to make draws on the line of credit to meet the payroll and made payments on the debt after February 5, 1987, the date on which Hanson was informed that the Bank would not grant his request for added funding and would not honor the commitment in future financing, Hanson waived any action for fraud and thereby condoned the fraud, as a result of which, there is no viable claim of fraud to submit to the jury.

The Court of Appeals rejected the Bank's contention in holding the maintenance of an action in tort for fraud is based on the acceptance of the contract and the claim is

not barred by mere acts of affirmance. In *Sanford Construction Company* v. *S & H Contractors, Inc.*, Ky., 443 S.W.2d 227 (1969), this Court held that a defrauded party who has substantially performed his contract before discovery of the fraud may go on with the performance and also recover damages. Where the terms of the contract were not wholly executory at the time the fraud was discovered, but had been performed, the claim for fraud and misrepresentation was the appropriate avenue.

The Bank suggests that Hanson's evidence of loss for the destruction of Hanson's construction business was too speculative and that, as a matter of law, the proof of damages does not meet the standard of reasonable certainty announced in *Pauline's Chicken Villa, Inc.* v. *KFC Corporation*, Ky., 701 S.W.2d 399 (1986). The basis for its assertion is that Hanson's expert witness, called to prove damages, rejected consideration of Hanson's history and thereby ignored the best available evidence. In *Pauline's Chicken Villa* this Court held that it cannot elucidate a single definition of "reasonable certainty."

In *Kellerman* v. *Dedman*, Ky., 411 S.W.2d 315 (1967), this Court quoted from the Wisconsin decision in *Essock* v. *Mawhinney*, 3 Wis.2d 258, 270, 88 N.W.2d 659, 664 (1958).

> [I]t is now generally held that the uncertainty which prevents a recovery is uncertainty as to the fact of the damage and not as to its amount and that where it is certain that damage has resulted, mere uncertainty as to the amount will not preclude the right of recovery. This view has been sustained where, from the nature of the case, the extent of the injury and the amount of damage are not capable of exact and accurate proof. Under such circumstances all that can be required is that the evidence with such certainty as the nature of the particular case may permit lay a foundation which will enable the trier of facts to make

> a fair and reasonable estimate and the plaintiff will not be denied a substantial recovery if he has produced the best evidence available and it is sufficient to afford a reasonable basis for estimating his loss.

In the case before us, the witness did establish his qualifications and the fact that the methods used by him are recognized methods for valuing companies. His methods did consider past performances of this company and its improving future of increasing work, its backlog, anticipated growth and other factors.

We conclude there was adequate competent evidence presented during the trial of the case to support submitting the instruction to the jury on the issue of compensatory damages.

The next claim of error is the charge by the Bank that the trial court erred in giving a jury instruction that it was the duty of the Bank to act in good faith. The Bank insists that since the notes signed by Hanson were demand notes, already due and subject to being called at any time without reason, it was improper for the trial judge to impose upon the Bank the added duty to act in good faith, a duty not imposed in the contract documents. We do not reach the issue of whether a duty of good faith is owed in calling a demand note. Under the instruction to the jury, the award of damages could only be made on a finding of fraudulent misrepresentation. The jury's finding of fraud alone supports the award. The instruction on fraudulent misrepresentation given by the court to the jury clearly and accurately defines the essential elements that Hanson must prove and the jury must find to establish a claim for fraudulent misrepresentation. The addition of the good faith instruction added nothing and, even if it were erroneously given, it is a harmless error.

This Court cannot accept the Bank's contention that since banking is an industry subject to strict federal and

state regulations that openly discourage, if not prohibit, it from making loan commitments and promises similar to those the jury determined were made in the case, that as a matter of public policy the banking industry should not be held liable when it attempts to cut its losses by discontinuing and cutting off the credit of customers it believes are a poor business risk.

The idea that any person or industry or enterprise would be immune from liability for fraud and deceit is not acceptable. *Bryant* v. *Troutman*, Ky., 287 S.W.2d 918 (1956).

> The law should not, and does not permit a covenant of immunity to be drawn that will protect a person against his own fraud. Such is not enforceable because of public policy. Language is not strong enough to write such a contract. Fraud destroys all consent. It is the purpose of the law to shield only those whose armor embraces good faith.

The Bank argues that Hanson established no basis for the award of punitive damages. In light of what has been said earlier in the opinion, we cannot accept such an argument. We have found that there is sufficient evidence and therefore reasonable grounds for submitting to the jury the issue of fraud and misrepresentation. Once the jury had found that the Bank intentionally misrepresented and deceived Hanson, an instruction on punitive damages should have been given and the jury afforded the opportunity to asses such sums as it considered appropriate. The trial court submitted instructions applying the factors set out in KRS 411.186. The constitutionality of this statute is not in issue in this case.

The case reaches this Court on the issue of the instructions by the trial court to the jury on punitive damages and on the issue of remittitur. The Court of Appeals found that since the jury's award of compensatory damages was substantial, it would by itself be a deterrent of future de-

ceptive practices and that in comparing the punitive damages assessed by the jury with the fraud that caused it, when taking into consideration the relevant statutory factors, the jury's award of punitive damages was disproportionate.

The court concluded that the award of punitive damages was the result of a failure in the instructions to identify a measure for fixing the amount of such damages. The court concluded that to the extent the award of punitive damages exceeded three times the compensatory damages, it was excessive and the excess should be remitted or a new trial ordered. This Court is unaware of any authority in this jurisdiction for court-ordered remittitur of punitive damages or for the fixing of the amount of such damages, and it will not here establish such precedent.

In *Pacific Mutual Life Insurance Co.* v. *Haslip*, ___ U.S. ___, 111 S.Ct. 1032, 113 L.Ed.2d 1 (1991), the United States Supreme Court reaffirmed its earlier ruling that an award of punitive damages does not violate the due process clause of the Constitution. That Court did identify the parameters the trial court and appellate court should apply in insuring that an award of punitive damages meets the test of due process. The Court held that instructions to the jury must define the purpose of punitive damages as punishment to the wrongdoer and as a deterrent to wrongdoers and others from such activities in the future and that post-trial procedures be in place and utilized by the trial court to scrutinize the award of such damages. The instructions here were adequate under *Haslip*.

The trial court instructed the jury in accordance with the provisions of KRS 411.184 and 411.186. The judge set forth in detail the definitions and standards the jury was to use in its deliberation in deciding whether punitive damages should be awarded and, if so, in what amount.

Such instructions are the only guidance that may be given the jury. Reasonable men and women will differ in determining the amount of exemplary damages, but so long as the jury's decision is based on competent evidence, is free of passion or prejudice, and is appropriately reviewed by the trial judge, we find no basis for substituting the Court's opinion in the place of the jury's.

In the present case, the jury was given an instruction that met the standards in *Haslip* and the post-trial review by the trial court of the punitive damages award conformed to the *Haslip* test. We find no basis in the Bank's argument.

This Court is mindful that Congress has enacted statutes that establish the amount of exemplary damages by permitting treble damages in certain cases. These caps are specified for certain statutory actions, not constitutionally protected actions. This Court is not inclined to enact law on the measure of punitive damages. Such is a matter for the legislature, provided it can be done consistent with our Constitution.

It is with equal caution that this Court does not substitute its opinion as to the amount of exemplary damages for that of the jury. It was the trial jury and trial judge who heard all the evidence and had the opportunity to see and hear the witnesses during the lengthy trial. The sanctity of the jury verdict is at the heart of out judicial system.

The procedures for review of the jury verdict are stated in CR 59.01. To assist the trial court in applying the test of determining whether a verdict is given under the influence of passion and prejudice, the "first blush rule" was adopted. *Davis* v. *Graviss,* Ky., 672 S.W.2d 928 (1984).

The Court of Appeals concluded, as does this Court, that in the award of punitive damages there is no basis on which to find the award was the product of passion or prejudice. But unlike the Court of Appeals, this Court

does not agree that the verdict of punitive damages is the result of a failure in submitting to the jury an instruction on a precise measure to be used in establishing the amount of such damages.

The Bank contends that by allowing evidence of the acquisition of American National Bank by First Kentucky National, Hanson was permitted to focus on the acquisition and thereby influence the jury in the award of compensatory and punitive damages. We cannot accept this assertion. We would agree with the Bank if the evidence of the takeover served no purpose other than to inflame or prejudice the jurors against outsiders. But here it was established that the takeover of American National Bank by First Kentucky was common knowledge and had been extensively advertised by both banks since 1985. More importantly, the evidence of the takeover is relevant and material in Hanson's proof of the acquisition, Hanson's claim of fraud would appear more a paranoid reaction than a meritorious claim. We see no reason to reject the standard of relevance announced in *Ford Motor Company* v. *Fulkerson*, Ky., 812 S.W.2d 119 (1991), that it is within the discretion of the trial judge whether the probative value of the evidence outweighs its inflammatory nature. There is nothing inflammatory in the evidence of the acquisition of American National Bank by First Kentucky that would unduly prejudice the jury against the Bank.

The decision and order of the Court of Appeals in remanding the matter to the trial court for remittitur of the punitive damages awarded or a new trial on those damages is reversed. The decision of the Court of Appeals affirming the judgment in the award of compensatory damages is affirmed.

All concur.

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COMMONWEALTH OF KENTUCKY
COURT OF APPEALS

89-CA-639-MR

AMERICAN NATIONAL BANK & TRUST COMPANY - *Appellant*

Appeal From Warren Circuit Court
v. *Honorable Joseph R. Huddleston, Judge*
Action No. 87-CI-318

HANSON CONSTRUCTION CO., INC.,
H. C. HANSON, VIRGINIA HANSON,
CONSTRUCTION ENGINEERS, INC., and
LUCILLE KINSLOW - - - - - - - - - *Appellees*

89-CA-690-MR (CROSS-APPEAL)

HANSON CONSTRUCTION CO., INC..,
H. C. HANSON, VIRGINIA HANSON, and
CONSTRUCTION ENGINEERS, INC. - - *Cross-Appellants*

Cross-Appeal From Warren Circuit Court
v. *Honorable Joseph R. Huddleston, Judge*
Action No. 87-CI-318

AMERICAN NATIONAL BANK & TRUST
COMPANY - - - - - - - - - - - *Cross-Appellee*

AFFIRMING IN PART, REVERSING IN PART, AND REMANDING

BEFORE: DYCHE, HAYES, and WILHOIT, Judges.

WILHOIT, JUDGE. H. C. Hanson Construction Company, H. C. and Virginia Hanson, and Construction Engineers, Inc.,

filed suit in April 1987 against American National Bank and Trust Company seeking compensatory and punitive damages from the Bank's termination of credit and calling of notes. The plaintiffs' trial theories included fraudulent misrepresentation, bad faith, emotional distress, breach of fiduciary duty, and oral contract. After the trial court entered directed verdicts on most of the alleged claims, the jury was instructed on fraudulent misrepresentation and the duty of good faith. The appeal by the Bank is from a judgment entered pursuant to the jury verdict awarding $1,065,000.00 compensatory damages and $5,775,000.00 punitive damages, which amounts were subject to set-offs for the unpaid principal and interest on the notes and an amount for attorney fees based on the loan documents. H. C. and Virginia Hanson, H. C. Hanson Construction Company, and Construction Engineers, Inc., cross-appeal from the portion of the judgment awarding the Bank attorney fees.

The trial was lengthy with the plaintiffs' proof taking about three weeks and the Bank's proof about two weeks. The following is not a summary of the evidence, but only highlights the facts necessary for an understanding of the issues presented in the appeal and cross-appeal.

Hanson Construction Company, owned by H. C. Hanson, was primarily involved in bridge construction. Mr. Hanson had been a customer of the Bank since the 1970's and Mr. David Chestnut was the Bank's loan officer who dealt with the Hansons from 1974 to at least 1982. Chestnut continued to communicate with the Hansons for the Bank after that date. Construction Engineers was a company formed by Mr. Hanson and others. Mr. Hanson eventually became the sole stockholder of that concern.

Like other businesses involved in the construction industry, Hanson Construction had problems generating a profit after 1982. The Bank continued to finance Hanson

through the lean years; by mid-year 1985 Hanson Construction had seven secured notes with the Bank, and Construction Engineers had an additional note. Hanson signed all the notes in both his corporate and personal capacities. Virginia Hanson signed a December 1983 note for $175,000.00 and also signed a personal guaranty for $125,000.00. The Bank was acquired by First Kentucky National Corporation in early 1985, an event which the Hansons characterize as changing their relationship with it.

Unbeknownst to the Hansons, after the acquisition their loans were reclassified substandard. Mr. Thomas Gurbach, a First National management trainee, was assigned the task of reviewing the Hansons' accounts. Gurbach authored what the Hansons refer to as the "Gurbach Memo" dated July 8, 1985. In the memorandum Gurbach recommended restructuring the Hansons' debt and giving Hanson a letter of credit and a restricted line of credit. The memo also contained a recommendation that the Bank secure additional collateral including a second mortgage on the Hansons' home. The Hansons highlight the portion of the memorandum where Gurbach indicated that "if ANB waited three to five months to foreclose it could come out with no loss due to the taking of additional collateral . . . . [T]his cash will have to come from the sale of his personal assets, in order to keep his company alive. . . . Overall this rewrite should reduce the Bank's potential loss and force Mr. Hanson to sell off his personal assets which undoubtedly would bring more than if the Bank auctioned them off." Hanson met with Gurbach and Mr. Willie McElroy, an officer at the Bank, to discuss the restructuring. Hanson informed Gurbach and McElroy that his wife, who had sole title to their residence, would not agree to a second mortgage on the house, and the meeting ended with no resolution. Hanson thereafter contacted Chestnut. Hanson testified that Chestnut told him that the Bank would finance

new work up to 20 percent of the contract amount at the Bank's interest rate in effect at the time of the contract, and the term for a line of credit would be one year to be renewed until completion of the work. Hanson drafted a letter July 15, 1985, in which he proposed a 15-year term note, $125,000 line of credit, and a $100,000 letter of credit secured by a second mortgage on the Hansons' residence and farm. McElroy informed the Hansons that the second mortgage would have to secure the Hansons' entire indebtedness to the Bank. Hanson testified that after his letter, Chestnut told him that with a restructuring and a second mortgage on the house and farm, the Bank would give Hanson Construction a $125,000 line of credit, provide financing for future contracts, and allow 15 years for repayment on the restructured loan.

The restructured loan was closed July 26, 1985. A February 1984 demand note was not included in the restructuring. Hanson started to read the closing documents, consisting of almost 100 pages, but the Hansons and their corporate secretary all testified that protests were made over the length of time it would take to read the material. Hanson testified that he was assured the documents were prepared in accordance with his understanding. As a consequence, Hanson did not read the closing documents. Contrary to Hanson's understanding, the restructuring did not include the alleged representations made by Chestnut. The restructured loan also did not conform to the "Gurbach memo" in all respects. The note signed for the restructured loan provided that no payments of principal or interest were due in December, January, or February of each year.

Hanson sought a loan from the Bank in the spring of 1986 to purchase equipment; that loan was denied. Hanson Construction obtained a subcontract to build two bridges in Campbell County, Kentucky, and Hanson successfully

obtained a $175,000 line of credit from the Bank for this project. A demand note representing the line of credit was signed in June 1986. Hanson subsequently subcontracted the smaller of the two bridges to Dixie Engineering, Inc., a company owned until December 1986 by Hanson, his wife, and their two sons. (In December 1986, all stock in Dixie was transferred to one of the sons.) The letter of credit for bonding from the Bank expired in July 1986, and Hanson associated with another Bowling Green contractor to obtain a performance bond for the Campbell County project.

Hanson Construction obtained a subcontract in October 1986 to build a bridge in Powell County. No financing from the Bank was sought for the subcontract at that time. The Bank maintained that Hanson Construction's fiscal 1986 statements contained material misstatements such that instead of the $3,500 profit alleged by Hanson, the company sustained a loss of over $94,000. Hanson approached McElroy in January 1987 for loans for Powell County and Lewis County subcontracts. The Executive Loan Committee of the Bank denied Hansons' request for funding for the Powell and Lewis subcontracts, as well as Hansons' request for an interest reduction. The committee also decided to preclude additional draws on existing lines of credit. After meeting with Hanson on February 6, 1987, the Bank allowed him to draw $7,000 a week for three weeks to meet payroll and seek alternative financing. Hanson made a quarterly interest payment February 6, 1987, on the 1986 demand note, and a payment on February 18 on the 1984 demand note. American demanded payment in full of the 1984 and 1986 notes on March 11, 1987. The restructure note of July 1985 was called after Hanson missed the next scheduled payment.

Hanson maintains that the Bank's actions in February and March 1987 forced Hanson Construction out of business on March 23, 1987. Negotiations between Hanson

and the Bank continued until Hanson filed suit April 13, 1987.

The Bank argues first that the loan documents must be enforced as written, and that evidence of any alleged representations by it to Hanson were not properly admitted at trial because of the parol evidence rule and the statute of frauds. We agree with the Bank that parol evidence would not be admissible to vary the terms of the documents by showing a previous or contemporaneous oral contract dealing with the same subject matter as the written documents. *See Citizens National Bank of Glasgow* v. *Damron*, 286 Ky. 43, 149 S.W.2d 762 (1941); *Childers & Venters, Inc.* v. *Sowards*, Ky., 460 S.W.2d 343 (1970). Apparently, the trial court also agreed inasmuch as it dismissed Hanson's claim based on oral contract. This evidence was admissible, however, to establish that Hanson had been induced to sign the documents through the fraudulent misrepresentation of the Bank's agents or employees. *See Bryant* v. *Troutman*, Ky., 287 S.W.2d 918 (1956). Neither *Klein* v. *Citizens Union National Bank*, 281 Ky. 650, 136 S.W.2d 770 (1940), nor *Citizens National Bank of Glasgow* v. *Damron, supra*, cited by the Bank in support of its position, involved fraudulent misrepresentation.

The Bank also argues that because the representations which it allegedly made concerning future financing, etc., were in themselves too indefinite to constitute an enforceable contract, *see Klein* v. *Citizens Union National Bank, supra*, Hanson could not rely upon those representations as a basis for establishing a claim for fraudulent misrepresentation. In support of this argument, it refers us to *Delcon Group, Inc.* v. *Northern Trust Corp.*, 187 Ill. App. 3d 635, 135 Ill. Dec. 212, 543 N.E.2d 595 (Ill. App. 2 Dist. 1989). In that case the court held that as a matter of law the plaintiffs could not rely on an alleged oral contract by which the Bank promised that it would provide them a

line of credit or equipment financing because essential terms of the contract were never agreed upon. The court reasoned that since the plaintiffs knew the alleged contract was too indefinite to be binding on any of the parties, they could not rely on it as binding the Bank. The appellees do not specifically respond to this argument.

The alleged misrepresentations made in this case are that the loan documents contained provisions for future financing of projects of up to 20 percent of the contract amount at the Bank's prevailing interest rate, a 15-year repayment schedule for the restructured loan, and that there would be no foreclosure as long as payments were current. Considering the relationship of the parties and what took place at the closing of the restructured loan according to the appellees' evidence, we cannot say as a matter of law that it would have been unreasonable to rely on the alleged representations by the Bank that these provisions were set out in the loan documents. *See Kreate* v. *Miller,* 226 Ky. 444, 11 S.W.2d 99 (1928). Similarly we do not find the provisions themselves were so indefinite that it would be unreasonable to rely upon their binding effect if, in fact, they had been placed in the written agreements.

Next, the Bank insists that because the Hansons elected to affirm the contract, any claim based upon the tort of fraud is waived and punitive damages may not be recovered. Furthermore, it argues that the election to affirm the contract is a condonation of the alleged fraud according to *Central States Fire Insurance Co. of Wichita, Kan.* v. *Holland,* 219 Ky. 727, 294 S.W. 489 (1927), *Castleman-Blakemore Co.* v. *Pickrell & Craig Co.,* 163 Ky. 750, 174 S.W. 749 (1915), *Perkins* v. *Jackson,* 276 Ky. 217, 123 S.W.2d 247 (1938), and *Dempsey* v. *Marshall,* Ky., 344 S.W.2d 606 (1961). The first three of these cases involve equitable actions to rescind or reform agreements and are not controlling in a tort action such as we have here. The

Dempsey case appears to be a tort case but supports the Hansons' position rather than the Bank's. Indeed, the maintenance of an action in tort for deceit "is based on the acceptance of the contract, it is not barred by mere acts of affirmance." W. Keeton, D. Dobbs, R. Keeton & D. Owen, *Prosser and Keeton on the Law of Torts* § 110 at 770 (5th ed. 1984); *see also Hampton* v. *Suter*, Ky., 330 S.W.2d 402 (1959).

In addition to the evidence concerning the assurances made by the Bank that the documents contained the omitted provisions, Hanson testified that he started to read the documents at the closing, but after protest from the Bank's attorney that "this would take all day," he stopped. Hanson also stated that before the closing, when he asked Chestnut if he should have his lawyer present, he was assured that that was not necessary. Further, Chestnut agreed with the statement "[i]f you can't trust your banker, who can you trust?" In light of this and other evidence, we are not prepared to say as a matter of law that Hanson's failure to read the documents was so imprudent as to bar recovery for deceit. *See United Talking Machine Co.* v. *Metcalf*, 174 Ky. 132, 191 S.W. 881 (1917); *Kreate* v. *Miller, supra; Cline* v. *Allis-Chalmers Corp.*, Ky. App., 690 S.W.2d 764 (1985).

Neither was Hanson's claim in tort for fraudulent misrepresentation barred by KRS 371.010. That statute bars an action upon "any agreement that is not to be performed within one (1) year." As stated in *Scott* v. *Farmers State Bank*, Ky., 410 S.W.2d 717, 722 (1966), "[o]ur statutes do not abrogate the common-law remedy for fraud merely because the fraudulent misrepresentations are by parol."

Next, the Bank argues that through the instructions the court erroneously imposed upon it the duty of good faith in calling the demand notes executed by the Hansons, and that a directed verdict in its favor on this issue should

have been entered. We need not concern ourselves with the question of whether a duty of good faith is owed in calling a demand note because any error in this respect could only have been harmless. Under the court's instructions the jury was permitted to award compensatory damages solely on a finding of fraudulent misrepresentation, even if it had not also found as it did that the Bank "breached its duty to deal in good faith . . . in the performance and enforcement of the loan agreements." The jury's finding of misrepresentation alone supports the award aside from any concomitant finding of bad faith.

The Bank contends that it was entitled to an instruction on estoppel. As no such instruction was requested or offered, the Hansons maintain the question is not properly before us under CR 51(3). The Bank insists that their tendered instruction on estoppel is found in Volume XV, at page 2205 of the record.

A proposed instruction followed by interrogatories to be answered by the jury are found at that page of the record. The proposed instruction is to the effect that the jury must find that the Hansons had breached their contractual and statutory duty if it determined that they had supplied false information to the Bank or withheld material information from it. The interrogatories questioned whether the Hansons' financial statements for October 1985 and 1986 were accurate and whether those statements "accurately represented the financial condition of the company." The instruction actually given by the court advised the jury that the Hansons had a duty to act in good faith. "Good faith" was defined as "honesty in fact in the conduct or transactions concerning which you have heard evidence." The jury was then asked whether the Hansons had violated their duty to deal with the Bank in good faith. If the jury answered affirmatively, then no recovery for the Hansons was permitted. From the argument of counsel, it

was made quite clear to the jury that if the Hansons had given the Bank inaccurate or materially incomplete information about their financial condition, they had not acted with honesty in fact.

We conclude that the factual question of whether the Hansons had dealt dishonestly with the Bank, and if so that they were estopped from recovery, was accurately and concisely presented to the jury through the instruction given. We find no reversible error in the court's failure to give the Bank's tendered instruction. *See Collins* v. *Galbraith*, Ky., 494 S.W.2d 527 (1973); *Cox* v. *Cooper*, Ky., 510 S.W.2d 530 (1974). We also believe that the question of whether the Hansons had acted honestly was properly submitted to the jury since there were material factual questions bearing on this issue. Of course, in light of what we have already said, we find no inconsistency in the trial court's directing a verdict in favor of the Bank on the written contract while submitting the tort claim for fraudulent misrepresentation to the jury, although the Bank would have us find otherwise.

At the close of the case for the Hansons, the court directed a verdict against them on their claims for emotional distress, physical injury, fiduciary duty and oral contract. The Bank then moved the court to immediately advise the jury that it need not consider those claims nor "take into consideration the testimony respecting those claims." The court denied the Bank's motion stating that it would wait until the end of the entire case to advise the jury of its directed verdict. At the close of all of the evidence, the Bank asked the court to give an instruction which "would literally instruct the jury" to return a verdict in favor of the Bank on each of the claims for which a directed verdict had been granted. The court declined to do this, and under our practice was not required to so instruct. *See* CR 50.01. No further request was made

about merely advising the jury of the directed verdict, and the court apparently never did. Accepting that it perhaps would have been better practice to have advised the jury of the directed verdict, we see no reversible error on this score.

The trial court did not abuse its discretion in permitting the witness Charles Cowles to testify. The Bank, which was permitted to depose Mr. Cowles before his testimony was presented to the jury, has failed to demonstrate any unfair prejudice by the admission of his testimony. *See Collins* v. *Galbraith, supra.* The Bank also contends that this testimony should not have been admitted because it contradicted a judicial admission already made by Hanson. Aside from the fact that the statement alleged to be a judicial admission is not so clear and unequivocal as to be considered such, *see George M. Eady Co.* v. *Stevenson*, Ky., 550 S.W.2d 473 (1977), the Bank has failed to show that this particular argument was presented to the court before the testimony was admitted. *See* CR 46; 76.12(4)(c)(iv).

The Bank argues that the court erred in submitting "a damage instruction to the jury when the evidence [of damage] was based on the loss of future profits," which it says were speculative at best. The matter of future profits arose, not because the Hansons sought recovery for them, but because future profits were used by the Hansons' expert witness as a factor in calculating the market value of the Hanson Construction Company at the time the Bank cut off its credit, allegedly forcing it out of business. The expert testified that this was an accepted method of evaluation, even that it was a method used universally and was "the most recognized method for valuing companies." The method he employed among other things, considered the past performance of the company; its then-improving situation; its likely profit in the year it ceased operation, based

upon reasonably projected revenue and expenses; and its backlog and conservatively anticipated growth in the future, based upon a number of factors. Considering this evidence presented as a whole, we find that it certainly supported an instruction on damages.

There is no merit to the Bank's position that because "[t]his is a contract case" it was error under KRS 411.184(4) to permit the jury to consider punitive damages. As stated previously, the case submitted to the jury, and upon which the punitive damages were awarded, is one in the tort of deceit.

The Bank also complains that the punitive damages which were awarded violated the fourteenth amendment to the United States Constitution as well as Sections 1, 2 and 14 of the Kentucky Constitution. The basis for this argument seems to be that the jury was given no standard by which to measure the amount of punitive damages it could or should award. While KRS 411.186 does provide for certain factors to be considered by a jury in awarding punitive damages it gives no guidance as to how to measure the amount which should be awarded. However, the Bank again fails to point out how this question has been preserved for our review, *see* CR 76.12(4)(c)(iv). From our review of this voluminous record, it does not appear the trial court was ever asked to incorporate into the instructions any standards governing the amount of punitive damages which the jury could award. The only objection we find to the punitive damage instructions is that the evidence was "not of sufficient quantity or quality to justify that." *See* CR 51(3).

The Bank's next contention is that since the award of punitive damages was so excessive that it failed to pass the "first blush rule" referred to in *Davis* v. *Graviss*, Ky., 672 S.W.2d 928 (1984), the trial court erred in not setting the award aside or ordering a remittitur. In *Davis* the

Kentucky Supreme Court explained that the "first blush rule" is a mechanism to assist the trial court in determining whether a jury's award of damages is so excessive as to appear to have been given under the influence of passion or prejudice under CR 59.01(d).

Formerly it was considered in this jurisdiction that punitive damages, in part at least, were "given as compensation to the plaintiff, and not solely as a punishment of the defendant." *Tennessee Central R. Co.* v. *Brasher's Guardian*, 29 Ky. Law Rep. 1277, 97 S.W. 349 (1906); *see also Louisville & N. R. Co.* v. *Ritchel*, 148 Ky. 701, 147 S.W. 411 (1912). The present view is that they are awarded solely to punish the defendant for his outrageous conduct and to discourage similar conduct. *See Ashland Dry Goods Co.* v. *Wages*, 302 Ky. 577, 195 S.W.2d 312 (1946). The change in theory appears to have occurred as the scope of damages that can be recovered by way of compensatory damages has expanded. Still, it should be recognized that punitive damages are not paid to the state treasury but to the injured party, and for that reason do still serve as a practical matter to compensate a successful plaintiff for such things as attorney fees for which he may not be entitled to recover by way of compensatory damages. Perhaps a more forthright rule would acknowledge that recovery for litigation expense is allowable as an element of punitive damages. This would have the virtue of giving the jury a more definite criterion for setting at least a portion of the punitive damage award. But, that is not now the law.

The law in this jurisdiction has long been that the amount of punitive damages to be awarded rests in the sound discretion of the jury with the limitation that the amount awarded cannot be so excessive as to indicate that it was made under the influence of passion or prejudice. Of equal importance, the amount must have some reason-

able relation to the injury and its cause, and not be disproportionate when compared to them. *See Louisville & N. R. Co.* v. *Roth*, 130 Ky. 759, 114 S.W. 264 (1908). However, the award need not bear any proportional relation to the amount of compensatory damages awarded. *See Hensley* v. *Paul Miller Ford, Inc.*, Ky., 508 S.W.2d 759 (1974).

Although it is impossible to measure with absolute certainty the amount of punitive damages, litigants must not be left to a jury's arbitrary will without remedy. *See Louisville So. R. Co.* v. *Minogue*, 90 Ky. 369, 14 S.W. 357 (1890). To permit an arbitrary award to stand would be to disregard Section 2 of Kentucky's Constitution.[1] The verdict is to be treated prima facie as the result of honest judgment on the part of the jury and the reviewing court is to exercise great caution in interfering with that verdict. *Minogue*, 14 S.W. at 358. If, however, the verdict can be accounted for only on the theory that it is the result of an improper sympathy or unreasonable prejudice, "it is one of the highest duties of a court to interfere." *Id.*

The damage award in *Davis* v. *Graviss, supra*, was for compensatory rather than punitive damages; however, in *Fowler* v. *Mantooth*, Ky., 683 S.W.2d 250 (1984), the court applied the holding in *Davis* to review a jury's award of punitive damages. It emphasized that insofar as appellate review of an award is concerned, the trial court's decision on excessiveness is presumptively correct, and the appellate court will reverse that decision only when the trial court has abused its discretion.

Whether the rule in *Mantooth* states a distinction without a difference from that in *Minogue* is not for us to say,

---

[1]Unlimited jury or judicial discretion in setting punitive damages would also raise a federal constitutional question. *See Pacific Mutual Life Insurance Co.* v. *Haslip*, U.S. ___, 59 U.S.L.W. 4157, 111 S. Ct. 1032 (March 4, 1991).

but it seems inescapable that to apply either, the appellate court must first determine whether the jury has abused its discretion in awarding punitive damages. How else can it be determined that the trial court has or has not abused its discretion in confirming or setting aside the jury's award?

We well understand the perplexity of the learned trial judge in attempting to apply our law with respect to punitive damages to the question of excessiveness. In doing this he was engaged in a less than exact science, although one not without fixed norms. It is apparent that he was well versed in the law on the subject; nevertheless, his ruling that the punitive damages award was not excessive appears ultimately to have been based upon consideration of the compensatory damages award and reliance upon a recent case in which Kentucky's Supreme Court had held that an award of punitive damages equalling 42 times the amount of the compensatory damage award was not excessive. It might well be in a given case that an award of punitive damages which is 42 times the amount of compensatory damages would be appropriate. It might well be that punitive damages considerably less than the amount of compensatory damages would also be appropriate in a given case. Nevertheless, the amount of compensatory damages simply has no direct relevance to the amount of punitive damages to be awarded in the sense that the punitive damages should be judged as some multiple or fraction of compensatory damages. Punitive damages should be measured by the injury inflicted and its cause, while taking into account the factors set out in KRS 411.186 and the purpose of such damages, which is to punish and deter similar tortious conduct.

The injury inflicted here was substantial. Under the jury's finding the Bank effectively destroyed the Hanson Construction Company as a result of its intentional tort. The evidence raised an inference that the Bank realized what would happen to Hanson, but acted to better its own

financial position through deceit. Further, the Bank did not act to remedy its misconduct. At the same time it should be considered that the injury inflicted was financial as opposed to the infliction of serious physical injuries or the loss of life or creating a danger of either.

The award of compensatory damages was substantial and would seem to have more than slight deterrent effect on future deceptive conduct by the Bank. Comparing the amount of punitive damages assessed with the injury sustained and the fraud which caused it, and taking into account the relevant statutory factors, we believe that the award made by the jury was so disproportionate that the trial court should have interfered. *See Louisville & N. R. Co.* v. *Roth*, 114 S.W. at 266. We do not conclude that the award was the product of passion or prejudice, but rather the result of the lack of a precise measure for fixing the amount to be awarded. The jury was instructed as to when punitive damages may be awarded and the purpose of such damages and the statutory factors to be considered in fixing the award. That is all of the guidance it had in setting an amount and about all that it could have under our system. Reasonable minds free of any passion or prejudice might differ greatly on what is an appropriate award based on the criteria to be considered. This might also be said of an award for pain and suffering. In any event, we still consider the award here to have been out of proportion to the injury and its cause.

The Bank states that under anti-trust and similar statutes there has been established "a benchmark punishment" of treble damages, and by implication it seems to suggest that this might be a standard by which to judge the punitive damages here. We do not think that necessarily follows, although it does constitute an expression of public policy with respect to certain wrongs involving commercial enterprises. We do conclude, however, that to the extent that the award of punitive damages in this case exceeded

an amount which would equal three times the compensatory damages, it was clearly excessive and the amount of excess should be remitted or a new trial ordered.

As to the other questions raised by the Bank, we find no reversible error, and we are not convinced on this record that the verdict was reached by the method condemned in *Louisville & N. R. Co.* v. *Marshall's Adm'x*, 289 Ky. 129, 158 S.W.2d 137 (1942), as constituting reversible error.

With respect to the cross-appeal, we find no abuse of discretion by the trial court in awarding attorney fees to the Bank since the Hansons elected to affirm their contract with the Bank and pursue their tort remedy.

The judgment of the trial court is affirmed with respect to the award of compensatory damages and is reversed as to the award of punitive damages, and this matter is remanded to that court for remittitur of the excess of punitive damages or the grant of a new trial as to those damages.

DYCHE, JUDGE, CONCURS.

HAYES, JUDGE, CONCURS IN PART AND DISSENTS IN PART AND FILES A SEPARATE OPINION.

HAYES, JUDGE, CONCURRING IN PART AND DISSENTING IN PART. I concur with the majority in affirming the trial court and dissent from that part that reverses and remands the issue of punitive damages. I would affirm the entire case. I know of no legal authority that permits a remand and/or remittitur on that issue.

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WARREN CIRCUIT COURT

DIVISION I

Civil Action No. 87-CI-318

HANSON CONSTRUCTION COMPANY, INC.,
H. C. HANSON, VIRGINIA HANSON, and
CONSTRUCTION ENGINEERS, INC. - - - *Plaintiffs,*

v.

AMERICAN NATIONAL BANK & TRUST
COMPANY - - - *Defendant, Counter-Claimant and Third-Party Plaintiff,*

v.

LUCILLE KINSLOW, - - - - *Third-Party Defendant.*

AMENDED TRIAL ORDER AND JUDGMENT

—Entered March 7, 1989

In accordance with the provisions of Rule 59 of the Kentucky Rules of Civil Procedure, the trial order and judgment entered in this action on January 27, 1989, is amended to read as follows:

This case was tried over a period of 24 days commencing on November 22, 1988, and ending on January 25, 1989.

The plaintiff corporations were present by their president, H.C. Hanson, and he and the plaintiff, Virginia Hanson, were present in person. All plaintiffs were represented by Charles D. Greenwell and David J. Kellerman.

The defendant, American National Bank & Trust Company, was present by its president, Robert Aldridge, and was represented by Douglas G. Sharp and Darell R. Pierce.

The third-party defendant, Lucille Kinslow, who was represented by Robert M. Alexander, having no direct interest in the outcome of the trial, was excused from participation in the trial.

The following jury was selected and sworn to try the case:

Brenda Martino	Kathleen Pankey
Roger Crabtree	Sandy Whitney
Judy Martin	Larry LaRue
Troy Tabor	Jack Butler
Orville Phelps	Lawrence White
Norma Harvey	Paula Stanley
Barbara Watt	Jon Tolbert.

Opening Statements were made by Mr. Greenwell for the plaintiffs and Mr. Sharp for the defendant.

The plaintiff called the following witnesses: H. C. Hanson (on 11/22, 23, 28, 29, 30 and 12/1/88), Virginia Hanson (on 12/1/88), Roger Dalton (on 12/1/88), Robert Aldridge (on 12/2/88), Thomas M. Gurbach (on 12/2/88), Robert Farris (by deposition on 12/2/88), Joan Hagan (on 12/7/88), David E. Chestnut (on 12/7/88), Willie Thomas McElroy (on 12/7-8/88), Jim Skaggs (on 12/9/88), Steve Hanson (on 12/9/88), Sandra Perry (on 12/9/88), Lee Anderson (by deposition on 12/9/88), James Scott (by deposition on 12/9/88), Dr. Douglas V. Austin (on 12/12/88), Richard T. Meyer (on 12/13-14/88) and announced closed (on 12/14/88).

The defendant moved for a directed verdict, which was sustained in part and overruled in part as appears of record.

The defendant called the following witnesses: Robert Aldridge (on 12/15/88), Herbert J. Smith (on 12/15/88), Virginia Hanson (by deposition on 12/15/88), H.C. Hanson (by deposition on 12/15-16/88), Deborah W. Williams (on 12/16/88), Larry Hinton (by deposition on 12/16/88), Carol

Sandidge (on 12/16/88), George Shaw (by deposition on 12/16/88) and Joyce Wilson (on 12/16/88), at which point the case was adjourned until January 10, 1989.

On January 10, 1989, the parties and counsel were present as before the recess. Mr. Greenwell, for the plaintiffs, and Mr. Sharp, for the defendant, made interlocutory statements.

The defendant then called the following additional witnesses: Joyce Wilson (on 1/10/89), Margaret Manning (on 1/10-11/89), John W. Saltzman, Jr. (on 1/10/89), Kent Kirby (on 1/11/89), John (Jack) Jenkins (on 1/11-12/89), James Cook (on 1/12/89), Tommy Jackson (by deposition on 1/12/89), Henry Faurest (on 1/12-18/89), Spencer A. Coates (on 1/19-20 and 23/89) and announced closed.

On rebuttal, the plaintiff called Joan Hagan (on 1/23/89) and Charles Cowles (on 1/23/89) and announced closed.

On rebuttal, the defendant recalled Spencer Coates (on 1/23/89) and announced closed.

The defendant moved for a directed verdict on the debt instruments and upon the plaintiffs' claims. The motions were sustained in part and overruled in part as appears of record and as hereinafter set forth.

The plaintiff moved for a directed verdict. The motion was overruled.

The parties having previously tendered proposed instructions, moved the Court to instruct the jury in accordance therewith. To the extent that the tendered instructions are not incorporated into the instructions given by the Court, the motions were overruled.

On January 24, 1989, the Court instructed the jury and closing arguments were made by Mr. Sharp for the defendant and Mr. Greenwell for the plaintiffs.

On January 25, 1989, Kathleen Pankey and Paula Stanley were selected as alternates and excused, and at

10:10 a.m., the jury retired to consider its verdict. Following its deliberations, at 2:15 p.m., the jury returned the following verdict in the form of answers to special interrogatories:

1. Have the plaintiffs established their claim against the defendant for fraudulent misrepresentation by clear and convincing evidence?

ANSWER: "Yes"

• • • • • • • •

2. Are you satisfied from the evidence that the defendant violated its duty to deal in good faith with the plaintiffs in the performance and enforcement of the loan agreements?

ANSWER: "Yes"

• • • • • • • •

3. Are you satisfied from the evidence that the plaintiffs violated their duty to deal in good faith with the defendant in the performance of the loan agreements?

ANSWER: "No"

• • • • • • • •

4. What sum do you find from the evidence will fairly and reasonably compensate the plaintiff, H.C. Hanson Construction Company, Inc., for the fair market value of the corporation on March 23, 1987?

ANSWER: "$1,065,000.00."

• • • • • • • •

5. What sum do you find from clear and convincing evidence should be awarded the plaintiffs as punitive damages?

ANSWER: "$5,775,000.00."

/s/ Roger D. Crabtree
Foreman

/s/	Roger D. Crabtree	/s/	J. Todd Tolbert
/s/	Jack Butler	/s/	Lawrence White
/s/	Sandy Whitney	/s/	Larry LaRue
/s/	Barbara Watt	/s/	Troy Tabor
/s/	Orville Phelps		
/s/	Norma F. Harvey		

At the request of the defendant, the jury was polled and when questioned, each juror who had signed the verdict indicated that it was his or her verdict as to each of the interrogatories answered.

In accordance with the verdict of the jury and the rulings of the Court made during the trial of this action, it is ORDERED and ADJUDGED as follows:

1. The plaintiff, H.C. Hanson Construction Company, Inc., shall recover from the defendant, American National Bank & Trust Company, the sum of $6,840,000.00, together with interest at 12% per annum, compounded annually, from and after entry of this judgment, until paid, less the sums awarded in paragraphs 2, 3, 4 and 5 below, and the costs of this action.

2. The defendant, American National Bank, shall recover from the plaintiffs, jointly and severally, the sum of $124,151.17, representing the principal balance of the February 17, 1984, note, the further sum of $25,139.17, representing interest on said note through December 13, 1988, and the interest on the principal balance at the rate of 10.5%, compounded annually, from and after December 14, 1988, until January 27, 1989.

3. The defendant, American National Bank, shall recover from the plaintiffs, jointly and severally, the sum of $364,929.44, representing the principal balance of the July 26, 1985, note, the further sum of $91,990.37, representing interest on said note through December 13, 1988, and interest on the principal balance at the rate of 11%, compounded annually, from and after December 14, 1988, until January 27, 1989.

4. The defendant, American National B. k, shall recover from the plaintiffs, jointly and severally, the sum of $67,048.09, representing the principal balance of the June 6, 1986, note, the further sum of $12,906.91, representing interest on said note through December 13, 1988, and interest on the principal balance at the rate of 10.5%, compounded annually, from and after December 14, 1988, until January 27, 1989.

5. The defendant, American National Bank, shall recover from the plaintiffs the sum of $101,385.00, which the Court has determined to be a reasonable attorney's fee for services rendered in collecting the notes referred to in paragraphs 2, 3 and 4 above.

6. The plaintiffs shall maintain in full force and effect, pending a final resolution of this action, a policy or policies of insurance issued by a company authorized to do business in the Commonwealth of Kentucky, insuring buildings located on the premises subject to the mortgages granted to the defendant against damage or destruction by fire, windstorm or other casualty, in an amount equal to the fair cash value of such buildings with the defendant named in said policies as an additional insured. The defendant shall be furnished with proof that said policy or policies of insurance have been issued and are in effect.

This 6th day of March, 1989.

/s/ Joseph R. Huddleston
Joseph R. Huddleston, Judge
Warren Circuit Court, Division I

Clerk, send copies to:
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Douglas G. Sharp
Darell R. Pierce
Stephen L. Hixson
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(2)

Supreme Court, U.S.
FILED
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OFFICE OF THE CLERK

No. 92-1522

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1992

AMERICAN NATIONAL BANK & TRUST COMPANY - - - - - Petitioner

versus

H. C. HANSON,
VIRGINIA HANSON,
H. C. HANSON CONSTRUCTION COMPANY and
CONSTRUCTION ENGINEERS, INC. - Respondents

Petition For A Writ Of Certiorari
To The Supreme Court Of Kentucky

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the Petitioner timely and properly developed a substantial federal constitutional issue in the state courts for this Court's review.

2. Whether the Petition should be granted where the Supreme Court of Kentucky unanimously affirmed the trial court's judgment against the Petitioner and expressly found that the jury instructions applying Kentucky's punitive damage statute and the post-trial review were sufficient in light of *Pacific Mut. Life Ins. Co.* v. *Haslip,* 111 S.Ct. 1032 (1991).

PARTIES TO THE PROCEEDING

The Respondents are H. C. Hanson ("Mr. Hanson"), Virginia Hanson ("Mrs. Hanson"), H. C. Hanson Construction Company, Inc. ("Hanson Construction") and Construction Engineers, Inc. (collectively "the Hansons").

The Petitioner, American National Bank & Trust Company ("ANB" or "Bank"), is a wholly-owned subsidiary of First Kentucky National Corporation ("FKNC"), which is a wholly-owned subsidiary of National City Corporation.

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No. 92-1522

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1992

AMERICAN NATIONAL BANK & TRUST COMPANY - - - - - - - - - - *Petitioner*

v.

H. C. HANSON,
VIRGINIA HANSON,
H. C. HANSON CONSTRUCTION COMPANY and
CONSTRUCTION ENGINEERS, INC. - - - *Respondents*

Petition For A Writ Of Certiorari
To The Supreme Court Of Kentucky

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

STATEMENT OF THE CASE

Respondents do not accept Petitioner's statement of the case. ANB's statement of the facts is replete with misstatements and omissions (Pet., 2-6).

This is a tort action for damages for fraud and deceit. After a twenty-four day trial, the jury concluded that ANB forced Hanson Construction to default on $3,670,000 in

contracts and through intentional fraud destroyed the company. ANB secretly planned and carried out its fraud against the Hansons during 1985, 1986 and 1987. The jury's verdict for $1,065,000 in compensatory damages and $5,775,000 in punitive damages was based on clear and convincing evidence and the jury's express finding of fraud. This is the first punitive damage case decided under Kentucky's new punitive damage statute, Ky. Rev. Stat. Ann. ("KRS") §§ 411.184 and 411.186 (Michie 1992) (effective July 15, 1988) (App. 1a-2a). The punitive damage instruction covered all the definitions, factors and guidelines for the jury outlined in the statute (App. 3a-8a). Special verdict interrogatories insured exactness with respect to the issues submitted and the jury's findings on those issues. Ky. CR 49.01.

ANB's Petition seeks review of a unanimous Supreme Court of Kentucky Opinion entered December 17, 1992, that affirmed the judgment against ANB based on the jury's verdict. *Hanson* v. *American Nat. Bank & Trust Co.*, 844 S.W.2d 408 (Ky. 1992) (Pet., 1a-16a). The Kentucky Supreme Court's Opinion gave careful consideration to *Pacific Mut. Life Ins. Co.* v. *Haslip*, 111 S.Ct. 1032 (1991). The Kentucky Supreme Court did not attempt to state all of the facts supporting the judgment but just the facts "necessary for an understanding of the issues presented" (844 S.W.2d at 411; Pet., 2a-4a). The Court's statement of the facts is incorporated by reference as an overview of ANB's fraud and deceit.

ANB's fraud was not limited to the inducement of a loan restructure as ANB implies (Pet., 5, 7). Instead, ANB, through a preconceived plan to defraud them, restructured the Hansons' loans on July 26, 1985, and then cut off their credit on February 5, 1987. The Hansons were good customers of ANB and never defaulted on any payment to ANB during their 15-year banking relationship. However, after FKNC took over ANB on February 11, 1985, ANB

included the Hansons' accounts within a whole tier of customer accounts that it reclassified as "problem" accounts and selected for termination. None of the customers, including the Hansons, were advised of the status of their accounts. If the Hansons and customers like them had been advised, they could have changed banks. However, ANB's secrecy and deceit denied them that opportunity.

ANB's plan for the Hansons was to restructure the Hansons' personal and business loans and take additional collateral, including a mortgage on Mrs. Hanson's house and farm, to improve its own position before it terminated their credit. The plan was concealed from the Hansons. However, it was documented in an internal bank memorandum dated July 8, 1985, that surfaced during discovery. The memorandum was identified and introduced at trial as the "Gurbach Memo" (App. 9a-16a). The author of the memo, Tom Gurbach, was a member of what FKNC and ANB called a "SWAT Team." FKNC sent the SWAT Team to ANB with a new president, Robert Aldridge, from First National Bank of Louisville on February 11, 1985. The Kentucky Supreme Court referred to the SWAT Team as a "task force" (844 S.W.2d, at 411; Pet., 2a-4a).

Aldridge had "orders" from FKNC to "clean up" the bank during 1985-1987. The SWAT Team's mission was to help Aldridge target accounts considered substandard and prepare plans to terminate them with a minimum loss to the Bank. It was in the context of this mission that the Gurbach Memo stated, in part:

> If the bank foreclosed today it would lose, on an optimistic basis, $140M if the building and land which he operates out of brings its full appraised value at auction and the equipment brings the value the Last Bid book indicates. The loss on a conservative basis would be closer to $250M. . . . However, if ANB waited three to five months to foreclose it could come out with no loss due to the *taking of additional collateral* set out earlier. . . . (emphasis added).

Consistent with the SWAT Team's mission, the Gurbach Memo concluded that:

> Overall this rewrite should reduce the bank's potential loss and *force Mr. Hanson to sell off his personal assets* which undoubtedly will bring more than if the bank auctioned them off. (emphasis added).

At a meeting on July 9, 1985, the SWAT Team approved the Gurbach Memo subject to a modification on timing (App. 17a-18a). The SWAT Team knew ANB had to finance Hanson Construction for at least a year before the cutoff. If a cutoff of credit forced the Hansons into bankruptcy within a year of the restructure, ANB knew that it could lose its newly acquired collateral because another creditor might claim a preference or fraudulent conveyance under sections 547 or 548 of the Bankruptcy Code. The SWAT minutes stated:

> We are going to wrap everything together, *take all collateral we can get* and we should be fairly well secured. We are going to give him a line of credit for this year. We will also be secured by contracts from counties he is working in. We have a $100,000 life insurance policy. Take a good look at this in September to see what his cash flow will be ($635,706.21). (emphasis added).

Gurbach and ANB's attorney, Larry Hinton, had the restructure documents ready for ANB on July 11, 1985. ANB's scheme for the termination of the Hansons' accounts was in place before Gurbach and McElroy met with Mr. Hanson on July 12, 1985 (Pet., 4).

ANB misrepresents that Mr. Hanson did not contact David Chesnut until after Mr. Hanson's letter of July 15, 1985 (Pet., 4). The misstatement is important because it implies that the restructure was Mr. Hanson's plan. It was not. Instead of Gurbach and McElroy, ANB used Chesnut to lure the Hansons into the restructure (Pet., 4).

Chesnut was the Hansons' loan officer and had been since 1974. Chesnut was the number two man at ANB after the change in ownership. ANB continued to use Chesnut as the Hansons' loan officer because the new management knew the Hansons trusted Chesnut. ANB exploited that trust to induce the Hansons into the restructure.

Chesnut and Mr. Hanson had meetings on July 13 and 15, 1985. Chesnut recommended that Mr. Hanson write the letter to supplement the financing that Gurbach, McElroy and Chesnut had all promised and agreed ANB would provide. For that reason Hanson's letter ". . . mentioned no other financing for future operations" (Pet., 4). Aldridge and Gurbach knew Chesnut was negotiating with Mr. Hanson. McElroy did not. Gurbach admitted he altered the July 15 letter without Mr. Hanson's knowledge to make it conform to the Gurbach Memo. On July 16, 1985, Chesnut told Mr. Hanson that ANB had approved his request for the supplemental financing. Mr. Hanson discussed it with his wife. On July 16 or 17, 1985, the Hansons agreed to the restructure based specifically on Chesnut's representations. ANB's omission of these facts is misleading.

Gurbach scheduled the closing for the restructure for July 26, 1985. The Hansons and the Corporate secretary for Hanson Construction attended the closing without counsel. They signed the restructure documents without reading them based on assurances of Chesnut and Hinton that the documents had been prepared just as agreed. Gurbach was present and knew the Hansons were deceived about the contents of the documents. The promised financing was omitted. ANB never intended to include it. The documents used were the same documents Gurbach and Hinton prepared and furnished to ANB on July 11, 1985. ANB implies that the documents were brief (Pet., 5). They were not. The legal documents consisted of 91 pages.

ANB skips the period from the restructure to January, 1987 for good reason (Pet., 5). During the interim ANB temporarily performed the promised financing it had omitted from the documents and later denied having made. At trial, banking experts agreed that without ANB's promises, the Hansons gave ANB additional collateral but got nothing in return. Absent ANB's promises, the restructure could not work. The Hansons had no reason to know ANB omitted its promises or to question ANB's performance of its promises before February 5, 1987. ANB's temporary performance concealed its fraud. In June, 1986, ANB established a line of credit for a new project with terms just as agreed. On January 20, 1987, Mr. Hanson left a meeting at ANB with the understanding that financing for the 1987 construction season was just a phone call away. He called ANB on February 2, 1987.

Before ANB cut off the Hansons' credit it made no complaint about the Hansons' performance. The Hansons were never in default. The Hansons had always paid as agreed. ANB ignored the turnaround in Hanson Construction's financial condition when it terminated the Hansons' credit on February 5, 1987. Hanson Construction's losses had dropped from $206,873.76 to $182,249.34 in July; from $182,249.34 to $174,555.67 in August; from $174,555.67 to $96,749.10 in September; and, at year end October 31, 1986, it was showing a profit. In addition, ANB was no longer exposed on a $100,000 letter of credit for bonding. Hanson Construction had paid ANB $117,000 more than required. The principal balance of the July 26, 1985 note was paid down to $484,685. ANB had collateral valued at $850,050.

ANB's cutoff was without default, without notice, and without demand. The cutoff at the beginning of the 1987 construction season was especially harsh. A three-year slump in the construction industry had ended. Hanson

Construction's future was bright. Its work had increased from $250,000 at the time of restructure to $3,670,000. ANB made no inquiry about bonding; in fact Hanson Construction had bonding (Pet., 6). ANB made no inspection of Hanson Construction's equipment; in fact it was well maintained (Pet., 6). ANB made no inquiry about expected profits; in fact Hanson Construction had cash flow to service the debt (Pet., 5-6). The credit analysis that ANB claimed was the basis for its cutoff did not consider the $3 million in new construction contracts Mr. Hanson acquired between May, 1986 and February, 1987 (Pet., 5-6). McElroy knew about the contracts but failed to tell the analyst as he should have. Also, McElroy altered bank records to show the maturity date for the June 6, 1986 line of credit note as February 1, 1987, instead of June 6, 1987.

ANB used the cutoff just as Gurbach had planned. ANB pressured the Hansons to sell off their property. ANB made no demand on February 5, 1987, because it wanted to hold out the possibility of further financing and prolong the pressure on the Hansons to make them cooperate with its plan. ANB had the Hansons' assets tied up. ANB had total control over the Hansons' credit. ANB knew that no alternative financing was available to the Hansons. ANB advanced $21,000 for three weeks' payroll, while it pretended to negotiate with the Hansons, to conceal its cutoff from prime contractors until it could grab another $41,500 in progress payments due Hanson Construction. ANB's cutoff was not for the reasons it claimed (Pet., 3, 5-6). It was in furtherance of ANB's secret plan.

ANB's demand on March 11, 1987, was an afterthought (Pet., 6). A call from the Hansons' counsel alarmed ANB's counsel. ANB's counsel triggered the demand. Payment on the restructure note was not due until March 26, 1987. However, by March 23, 1987, ANB's fraud had forced Hanson Construction out of business. The company was destroyed.

The Hansons introduced evidence of ANB's losses during 1985-1987 to show that ANB's termination of their accounts was because of its own financial condition, not the Hansons' financial condition as ANB claimed. ANB's response revealed the motive for ANB's fraud, the duration of its fraud, the concealment of its fraud, the magnitude of the harm, ANB's awareness of the harm, and ANB's failure to take any action to mitigate the harm.

ANB's president, Aldridge, admitted that the termination of the Hansons' credit was just part of a larger scheme he put in effect at ANB during 1985-1987 to clean up the bank. Up to a 1,000 accounts were affected. Aldridge revealed he had "orders" from FKNC to charge off the accounts "with a minimum loss to the bank."

Aldridge testified that during 1985-1987 he used every penny of ANB's profits, and more, to cover the resulting losses. He had assisted FKNC with the purchase of ANB and expected the losses. They were planned for in the purchase. Aldridge admitted that he knew the termination of customer accounts would be "mean and nasty" and had to be kept secret from the Bowling Green community. Otherwise, no one would bank at ANB. Because of his knowledge, when FKNC asked Aldridge to be president of ANB, he refused—twice. Aldridge refused to be president of ANB until FKNC agreed to pay him a higher salary and send ANB money to cover losses if they exceeded ANB's profits. At the end of 1986, FKNC had to send $2 million to ANB to cover extra losses so Aldridge could finish his so-called "clean up" in early 1987.

Aldridge boasted about his "clean up." He terminated about $11 million in customer accounts and recovered $8.26 million of the losses from tax credits and sales of collateral which secured the terminated customer accounts. ANB's net loss, $2.74 million, was less than he and FKNC had expected. Aldridge admitted that others could have run ANB differently.

ANB showed no remorse for its misconduct. Instead, ANB attempted to intimidate the Hansons' counsel (App. 19a-25a). ANB's trial strategy was to disclaim the Gurbach Memo, deny that ANB had pre-planned the termination of the Hansons' accounts, and assert vindictive counter charges of fraud and bad faith against the Hansons. Its tactics failed.

REASONS WHY THE PETITION SHOULD BE DENIED

1. ANB Did Not Timely and Properly Develop a Constitutional Issue in the State Courts For This Court's Review.

ANB has failed to comply with Sup. Ct. R. 14.1(h). It also ignored a similar rule in Kentucky. Civil Rule 76.12(4)(c)(iv) ("[Appellant's brief] . . . shall contain at the beginning of the argument a statement with reference to the record showing whether the issue was properly preserved for review, and if so, in what manner."). ANB did not demonstrate to the appellate courts of Kentucky that it had preserved a constitutional issue there, nor has ANB made such a showing here. For good reason. ANB did not preserve for review by the Kentucky appellate courts, or by this Court, the federal constitutional issues it now attempts to raise. ANB's amended answer contained only the following pallid assertion:

> 2. This answering Defendant raises as an affirmative defense the bar under the Constitution of the United States and the Constitution of Kentucky, of the imposition of punitive damages herein.

This generic defense makes no mention of the Fourteenth Amendment and is insufficient to raise and preserve a constitutional issue for this Court. *Bankers Life & Casualty Co.* v. *Crenshaw*, 486 U.S. 71, 77 (1988) ("A party may not preserve a constitutional challenge by generally invoking the Constitution in state court and awaiting review in this Court to specify the constitutional provision it is relying upon.").

Nor did ANB preserve a challenge to the constitutionality of Kentucky's punitive damage statute, KRS §§ 411.184, 411.186, in the Kentucky courts. The Kentucky Court of Appeals called attention to ANB's failure:

> The only objection we find to the punitive damage instructions is that the evidence was "not of sufficient quantity or quality to justify that."

The Supreme Court of Kentucky noted: "The trial court submitted instructions applying the factors set out in KRS §411.186. The constitutionality of this statute is not in issue in this case." (844 S.W.2d at 415; Pet., 12a). Again, there is a good reason why ANB did not challenge the statute. ANB urged the trial court to incorporate the statute in the Court's instructions to the jury. It has admitted in its Petition:

> The Bank did not object at trial and does not raise here the question of whether the punitive damage instruction actually given to the jury was correct. That instruction was a correct and accurate representation of Kentucky's punitive damage statute, Ky. Rev. Stat. Ann. § 411.186 (Michie 1992).

(Pet., 11).

Nevertheless, ANB complains to this Court that the trial court erred when it refused to instruct the jury about claims the trial court had dismissed on ANB's motion for a directed verdict. This "directed verdict issue" is one involving Kentucky evidence, Kentucky procedure and the trial court's discretion. Ky. CR 50.01 ("The order of the court granting a motion for a directed verdict is effective without any assent of the jury."). Moreover, ANB waived the issue in the trial court. The Kentucky Court of Appeals described the waiver: "No further request was made about advising the jury of the directed verdict, and the [trial] court apparently never did." (Pet., 27a). The Supreme Court of Kentucky added that the special verdict

interrogatories the trial court used to instruct the jury "best prevents the jury from considering immaterial issues and submits to the jury only the appropriate contested issues" (844 S.W.2d at 412; Pet., 5a-6a). If there was any risk, and there was none, that the jury might draw improper inferences from the evidence or the court's instructions, under Kentucky practice it was the responsibility of ANB's counsel to address the risk in closing argument. *Collins* v. *Galbraith*, 494 S.W.2d 527, 531 (Ky. 1973). *Ford Motor Company* v. *Fulkerson*, 812 S.W.2d 119, 122 (Ky. 1991) ("This case illustrates why we caution against instructions getting into evidentiary matters, subquestions which better practice suggests should be omitted from the instructions and left to the lawyers to flesh out in closing arguments.").

The constitutional "spin" that ANB tries to put on the "directed verdict issue" was not passed upon in the Supreme Court of Kentucky. The constitutional spin is merely an afterthought. It cannot be properly asserted here. Rule 14.1(h); *Crenshaw, supra.* Considering ANB's own waivers and admissions, there are no special or important reasons to grant ANB's Petition. Sup. Ct. R. 10.

2. This Case Is Not Appropriate For Review in This Court Because the Facts Involved in ANB's Intentional Fraud and the Facts Which Justified the Jury's Punitive Damage Award Are Too Case Specific.

This is an extremely fact specific fraud case. ANB's failure to accurately and fully set forth the facts is reason alone to deny the writ. *United States* v. *Johnson*, 268 U.S. 220, 227 (1925) ("We do not grant a certiorari to review evidence and discuss specific facts."). All of the trial court proceedings before, during, and after the twenty-four day trial were videotaped. Thirty-one witnesses testified. The exhibits were voluminous. The record has not been transcribed.

A review by this Court would involve questions of evidence and application of familiar legal principles. The jury's factual findings are based on special verdict interrogatories and are supported by clear and convincing evidence. A review merely to confirm settled principles of law would be of little or no public importance. Stern, *Supreme Court Practice*, §4.17 at 223 (6th Ed. 1986).

3. At ANB's Request, the Trial Court Instructed the Jury in Accordance With Kentucky's New Punitive Damage Statute and Provided Pre-Verdict Safeguards Which Were More Than Sufficient to Satisfy Constitutional Due Process.

The Kentucky legislature enacted a new statutory scheme for punitive damages, KRS §§ 411.184 and 411.186, after the Hanson's claim arose. This case is the first to apply the new statute. The statute specifies and limits the type of misconduct for which punitive damages may be claimed. The statute also incorporates standards and guidelines that limit jury discretion as to the award and amount of punitive damages. The trial court instructed that before the jury could even consider punitive damages, it had to find that the Hansons had proven the six elements of fraud against ANB by "clear and convincing evidence" (App. 3a-4a).

With respect to the jury's discretion to award punitive damages, the trial court incorporated the following statutory standards and guidelines in its instructions: (1) the "clear and convincing evidence" standard; (2) the definitions of the misconduct ("oppression," "fraud," or "malice") required for punitive damages; (3) the specific intent that must be shown for each type of misconduct; (4) the purposes of punitive damages, namely, to punish the defendant and to deter it and others from similar misconduct in the future; and, (5) the discretion of the jury to award punitive damages in addition to compensatory damages.

The trial court instructed that if the jury determined to award punitive damages, it should consider the following additional factors in determining the amount: (1) the likelihood that serious harm would arise from the defendant's misconduct; (2) the degree of the defendant's awareness of that likelihood; (3) the profitability of the misconduct to the defendant; (4) the duration of the misconduct; (5) any concealment of the misconduct by the defendant; and, (6) any actions by the defendant to remedy the misconduct once it was known to the defendant.

Finally, the trial court submitted the case to the jury on special verdict interrogatories pursuant to Ky. CR 49.01. The Kentucky rule follows FRCP 49(a). Ky. CR 49.01 is designed to insure exactness of the issues the jury is permitted to decide and the jury's findings on those issues. The jury returned special verdicts for fraud and for punitive damages. Both verdicts were based on clear and convincing evidence.

The form and content of the trial court's instructions satisfied constitutional due process. The Kentucky punitive damage statute and the trial court's instructions afforded ANB more *pre-verdict* safeguards and due process protection than the defendant in *Pacific Mut. Life Ins. Co.* v. *Haslip,* 111 S.Ct. 1032 (1991) had under Alabama law. The trial court, the Court of Appeals, and the Supreme Court of Kentucky all agreed that: the jury was properly instructed (Pet., 5a-6a, 14a); the evidence supported the jury's verdict against ANB on liability for compensatory and punitive damages (Pet., 11a-12a); and the jury's verdict for punitive damages was not the result of passion or prejudice (Pet., 14a).

There are no special and important reasons to grant ANB's Petition. The Supreme Court of Kentucky considered and applied *Haslip* when it reviewed and unanimously affirmed the trial court's judgment.

4. The Trial Court's Post-Verdict Review and the Final Appellate Review by the Supreme Court of Kentucky Were More Than Sufficient to Satisfy Constitutional Due Process.

ANB's representation that "[t]his Court has consistent with *Haslip*, granted review and reversed in at least eleven cases" is grossly misleading (Pet., 10). None of the cases were reversed. This Court vacated and remanded the cases for review by the lower courts in light of *Haslip*. The Supreme Court of Kentucky has already conducted such a review: "In the present case, the jury was given an instruction that met the standards in *Haslip* and the post-trial review by the trial court of the punitive damages award conformed to the *Haslip* test." (844 S.W.2d at 416; Pet., 14a). ANB's reliance on Sup. Ct. R. 10.1(b) as a reason for review in this case is misplaced (Pet., 10). There are no special and important reasons for this Court to conduct a further review or to require the Supreme Court of Kentucky to repeat its review.

Kentucky's statutory scheme for the assessment of punitive damages, as applied by the trial court and as explained and applied by Kentucky's highest court, provides far more safeguards and far more effective safeguards for protection of due process than did the Alabama common law method which the majority in *Haslip* found was constitutionally sufficient. In this case, ANB was afforded pre-verdict safeguards and the "clear and convincing evidence" standard that was suggested in the *Haslip* dissent.

The trial judge, who is now a judge on the Kentucky Court of Appeals, conducted a lengthy hearing on ANB's post-trial motions for judgment notwithstanding the verdict, new trial and remittitur on February 27, 1989. Before the hearing he had read all the briefs and all the authorities submitted, as well as others from his own research. The judge displayed the volumes of authorities he

had considered and stated on the record at the hearing that the handwritten notes and highlights on the authorities were his. He was fully aware of the evidence presented during the lengthy trial and ANB's counsel knew it. The trial court invoked the standards and discretion afforded to the trial court by Ky. CR 50.02, 50.03, 59.01, and 61.02.

ANB's representations that the trial court exercised no discretion and thought it had no discretion to protect ANB are false (Pet., 15). ANB has unfairly quoted the trial court out of context (Pet., 14-15). An examination of the trial court's entire statement reveals that it was supplying a rationale for its rejection of ANB's argument for a cap or multiple to limit punitive damages. Immediately after the comments quoted in the Petition, the trial judge stated:

> For some time defendants have advocated a stiffening of the standards for awarding punitive damages and the legislature responded to that and I did instruct under that statute although I still have some reservations as to whether or not it applied to this case. In other words I'm not sure the defendant was entitled to the more stringent rule that I instructed under. Likewise, I'm not sure the defendant was entitled to the rule under the fraud—fraudulent inducement part of the instructions that proof had to be by clear and convincing evidence but it seemed to me at the time that since the statute required that for punitive damages the case law required it for fraud that I ought to be consistent I ought to put that standard in for both and I did.

At the conclusion of the post-trial hearing the trial court further exercised its discretion by upholding the jury's verdict and denying ANB's motions:

> I've determined that I am going to overrule the motion for judgment notwithstanding the verdict. I'm also going to overrule the motion for remittitur. I will

> prepare an appropriate order, I will prepare a judgment in accordance with the discussions we had earlier today.

(Post-Trial Hearing, February 27, 1989). On March 9, 1989, the trial court entered its order denying ANB's motions for judgment notwithstanding the verdict, for remittitur, and for new trial.

The trial court's rationale for denying ANB's post-trial motions is consistent with Kentucky law. *Horton* v. *Union Light, Heat & Power Co.*, 690 S.W.2d 382, 385 (Ky. 1985) ("The role of the jury in interpreting the evidence and finding the ultimate facts is an American tradition so fundamental as to merit constitutional recognition. U.S. Const. Amend. VII; Ky. Const. Sect. 7"). The trial court's rejection of a cap or multiple on punitive damages was a harbinger of *Haslip*, which had not yet been decided. *Haslip*, 111 S.Ct. at 1043 ("We need not, and indeed we can not, draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable. . . .") (emphasis added).

Kentucky's legislature has asserted its interest and has determined that punitive damage standards and safeguards are to be applied before the jury's verdict. KRS §411.186(2) ("If *the trier of fact* determines that punitive damages should be awarded, *the trier of fact* shall then assess the sum of punitive damages. In determining the amount of punitive damages to be assessed, *the trier of fact* should consider the following factors. . . .") (emphasis added). The appellate review process in Kentucky is not a trial de novo; in this case, the Supreme Court of Kentucky determined that statutory and common law standards were properly applied by the trial court. Kentucky's highest court did not find new facts, create a new standard or apply its own yardstick.

ANB misstates Kentucky law (Pet., 15-16). The Supreme Court of Kentucky conducted a thorough review of the record, in accordance with the principles set forth in *Davis* v. *Graviss*, 672 S.W.2d 928, 933 (Ky. 1984) (". . . these rules charge us with the *responsibility to review the record* and decide whether, when viewed from a standpoint 'most favorable' to the prevailing party, there is evidence to support the verdict and judgment. *Rogers* v. *Kasden*, 612 S.W.2d 133 (Ky. 1981).") (emphasis added). *Wal-Mart Discount City* v. *Meyers*, 738 S.W.2d 841, 845 (Ky. Ct. App. 1987) ("Viewing the evidence in the light most favorable to [plaintiff] as we are required to do, we conclude that the evidence adduced amply supports the jury's award. That being so, we are not free to set that award aside on the ground of excessiveness."). The Kentucky Court of Appeals recognized: "The damage award in *Davis* v. *Graviss*, *supra*, was for compensatory rather than punitive damages; however, in *Fowler* v. *Mantooth*, 683 S.W.2d 250 (Ky. 1984), the court applied the holding in *Davis* to review a jury's award of punitive damages." (Pet., 30a).

ANB's criticism of Kentucky's "first blush" doctrine is hypocritical (Pet., 16-17). ANB invoked the "first blush" doctrine at three levels of the Kentucky court system. In Kentucky, the "first blush" doctrine is a valuable tool to assist the trial court in post-trial review. It is not an arbitrary concept. In *Commonwealth, Dept. of Highways* v. *Friend*, 500 S.W.2d 405, 406 (Ky. 1973), Kentucky's highest court defined "first blush" as follows:

> "First blush" is simply a summary determination that a verdict is unsupported by evidence of probative value. It stems from a sense of shock that such a verdict could have resulted from the evidence heard, a conviction beyond doubt by the court that the jury, lacking substantial evidence of probative value, was motivated by passion, prejudice or other improper factors and the resulting verdict is shocking and outrageous. In

> making this determination the court can draw upon its own knowledge and experience and the common experience of humankind generally.

"First blush" is the defendant's ultimate safeguard; it is never invoked in favor of the plaintiff. It is ironic that ANB would attack it here after having relied on it in the Kentucky courts.

Fowler v. *Mantooth, supra* at 253, best describes the function of Kentucky's appellate courts in a punitive damage case:

> The appellate court will reverse only when it can be said that the trial court has "clearly erred", i.e., abused its discretion, in refusing to set aside the award as excessive.

The concurring opinion observed:

> The jury is the arbiter of the amount to be allowed. The verdict of a properly instructed jury as to punitive damages should not be set aside unless it can be held that no reasonable juror, on the basis of the evidence presented, could have reached such a verdict, and therefore the verdict reached must necessarily have resulted from bias or passion on the part of the jurors.

Id. at 254.

In *Louisville & N.R. Co.* v. *Roth,* 114 S.W. 264, 266 (Ky. 1908), the Kentucky appellate court made clear its determination to scrutinize the facts and circumstances of each case:

> It is not practicable to say, even approximately, what amount of punitive damages a jury may assess in a case where this character of damages may be allowed. It is even more difficult of approximation and ascertainment than the correct measure of compensatory damages in personal injury cases. In the very necessity of things the amount must depend upon the facts and circumstances of each particular case. And

> so the amount that may be awarded as punitive damages must necessarily be left to the sound discretion of a jury . . .

Nevertheless, the Supreme Court of Kentucky does not hesitate to reverse and order a judgment notwithstanding the verdict when it concludes "that the verdict of the jury was without sufficient evidentiary basis." *National Collegiate Athletic Association* v. *Hornung*, 754 S.W.2d 855, 860 (Ky. 1988).

A comment in *Judicial Assessment of Punitive Damages, The Seventh Amendment, and the Politics of Jury Review*, 91 *Columbia Law Review* 142, 181 (1991) is therefore apropros:

> A state-created procedure, however, "is not subject to proscription under the Due Process Clause unless 'it offends some principle of justice so rooted in the traditions and conscience of our people as to be ranked as fundamental.'" [citations omitted] Under that standard, jury discretion in tort cases is more likely to be required by due process, given the jury's historical and constitutional role in American law, than prohibited by it.

If an appellate court could unilaterally take away the verdict of a properly instructed jury, which was rendered without passion or prejudice and which was strengthened by the trial court's denial of post-trial motions, then the jury would be stripped of the fact finding role inherent in the traditional jury trial and its function would be nothing more than advisory.

The Kentucky legislature and the Supreme Court of Kentucky have acted in harmony with the Seventh Amendment of the Constitution of the United States which states that ". . . no fact tried by a jury shall be otherwise reexamined in any court of the United States, than according to the rules of the common law." "The general rule bottomed deeply in belief in the importance of state control of state judicial procedure, is that federal law takes

state courts as it finds them'." *Howlett* v. *Rose,* 496 U.S. 356, 372 (1990). There are no special and important reasons for this Court to grant ANB's Petition.

5. The Jury's Verdict for Punitive Damages Was Rational and Reasonably Related to the Need to Punish ANB for Its Fraud and to Deter ANB and Others From Similar Misconduct in the Future.

The jury's punitive damage verdict of $5.775 million took less from ANB than ANB took from the Hansons and the Bowling Green, Kentucky community. ANB's own president testified that he terminated $11 million in accounts and recovered $8.26 million of the losses from tax credits and sales of the collateral that secured the accounts. In closing argument, counsel for the Hansons requested $10 million for punitive damages.

The record provides reasons to believe the jury's verdict of $5.775 million for punitive damages was so conservative that the public's interest in the "punishment" and "deterrence" of fraud was not fully served. *Fowler* v. *Mantooth,* at 253:

> To relate excessiveness of the award only in terms of its reasonable relation to the injury sustained, is to tell only half the story. . . . But the fatal flaw is that this analysis leaves out of consideration the character of the act. . . . An award of punitive damages need not bear reasonable relation to actual damages . . . if the claimant's evidence regarding the character of the act, meaning the extent of conscious wrongdoings, is sufficient to sustain the award.

At a post-trial hearing, ANB's counsel admitted ". . . quite frankly I'm told by the accountants that the reason Mr. Greenwell's Judgment is not disclosed [in financial statements] is *based upon the size, it's not material*" (emphasis added).

ANB did not request the trial court to include "net worth" as a factor in the instruction as Ky. CR 49.01 required; ANB did not assert the issue in its prehearing statement of appeal as Ky. CR 76.14(6) required; ANB did not assert the issue in its motion for discretionary review in the Supreme Court of Kentucky as Ky. CR 76.20(3)(d) required; and ANB cannot rely on the issue here. Sup. Ct. R. 14.1(h). After the Supreme Court of Kentucky rendered its opinion on December 17, 1992, ANB paid the judgment on December 24, 1992, less interest and penalties ANB disputes.

It is difficult to imagine anything more repugnant in the business world than a group of bankers, calling themselves a "SWAT Team," taking over a community bank and implementing a clandestine scheme to deliberately defraud the established customers of additional collateral before terminating their accounts. As Mr. Hanson stated to David Chesnut the morning of the closing for the restructure on July 26, 1985: "If you can't trust your banker, who can you trust?"

In Kentucky, fraud is recognized as the most insidious of all torts. *Kreate* v. *Miller,* 11 S.W.2d 99, 102 (Ky. 1928). It involves the wrongdoer's state of mind. It is preconceived and deliberate. It exploits and abuses confidences. It is concealable. It can be ongoing. It is difficult to discover and, if discovered, most difficult to prove. *Prosser on Torts,* §107, at 741 (4th Ed. 1971) ("The intent which underlies an intentional misrepresentation is a more complex matter than the relatively simple intention in the case of assault and battery.").

There is no case where the proof and culpability for the tort converges more closely with the proof and culpability for punitive damages than a case involving a scheme of fraud and deceit. *Head* v. *Oglesby,* 194 S.W. 793, 797 (Ky. 1917) ("[T]he transaction throughout is reeking with deceit, fraud and misplaced confidence . . ."); *Walker* v. *Sheldon,* 179 N.E.2d 497, 499 (N.Y. App. 1961) ("Exemplary damages are more likely to serve their desired pur-

pose of deterring similar conduct in a fraud case . . . than in any other area of tort.").

In its common law and in its statutes, Kentucky has expressed its interest in the use of punitive damages to punish and deter fraud. Compensatory damages are not a deterrent. *Tyson* v. *Ewing*, 26 Ky. 185, 3 J.J. Marsh 185 (1830). By legislative definition "punitive damages . . . means damages, other than compensatory and nominal damages, awarded against a person to punish and discourage him *and others* from similar conduct in the future" KRS §411.184(f) (emphasis added). Kentucky is among the jurisdictions that recognize general deterrence as a purpose for punitive damages. On the facts in this case it is not enough to deter ANB alone. The record is clear that FKNC, ANB's new parent, ordered and funded ANB's fraudulent, malicious and oppressive misconduct. Over-deterrence is not a factor in this fraud case. In light of ANB's fraud, the need for deterrence of "others" cannot be ignored.

Kentucky's highest court has determined that the state's interest in the punishment and deterrence of fraud is consistent with the due process considerations set forth in *Haslip*. There are no special or important reasons for this Court to grant ANB's Petition.

CONCLUSION

After a 24-day trial, a Kentucky jury, instructed in accordance with Kentucky's new punitive damage statute, found that there was clear and convincing evidence of ANB's fraud and imposed punitive damages that were approximately five times the amount of compensatory damages. The destruction of the Hansons' business by ANB was a result of ANB's larger scheme to minimize its losses in the Bowling Green, Kentucky community. The punitive damage verdict was less than the amount ANB's president boasted he extracted from the community, on orders of ANB's parent.

After an exhaustive review of the facts and the law, the trial court entered judgment in accordance with the verdict. The Supreme Court of Kentucky determined that the punitive damage judgment was proper under Kentucky law. Kentucky's highest court considered *Haslip* in its appellate review and specifically found that the jury instructions applying Kentucky's punitive damage statute and the post-trial review satisfied constitutional due process. ANB was afforded more due process, pre-verdict and on appellate review, than the defendant in *Haslip* was afforded under Alabama law.

Kentucky's legislature and Kentucky's highest court have expressed Kentucky's displeasure with the secret and insidious tort of fraud; both have expressed Kentucky's interest in punishing and deterring fraud by punitive damages. Yet, ANB would have this Court ignore the two-fold assertion of Kentucky's interest. ANB would have this Court restructure Kentucky's appellate practice. ANB would have this Court erode the principles of federalism.

Respondents pray that ANB's Petition be promptly denied.

Respectfully submitted,

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APPENDIX

411.184 Definitions; punitive damages; proof of punitive damages

(1) As used in this section and KRS 411.186, unless the context requires otherwise:

(a) "Oppression" means conduct which is specifically intended by the defendant to subject the plaintiff to cruel and unjust hardship.

(b) "Fraud" means an intentional misrepresentation, deceit, or concealment of material fact known to the defendant and made with the intention of causing injury to the plaintiff.

(c) "Malice" means either conduct which is specifically intended by the defendant to cause tangible or intangible injury to the plaintiff or conduct that is carried out by the defendant both with a flagrant indifference to the rights of the plaintiff and with a subjective awareness that such conduct will result in human death or bodily harm.

(d) "Plaintiff" means any party claiming punitive damages.

(e) "Defendant" means any party against whom punitive damages are sought.

(f) "Punitive damages" includes exemplary damages and means damages, other than compensatory and nominal damages, awarded against a person to punish and to discourage him and others from similar conduct in the future.

(2) A plaintiff shall recover punitive damages only upon proving, by clear and convincing evidence, that the defendant from whom such damages are sought acted toward the plaintiff with oppression, fraud or malice.

(3) In no case shall punitive damages be assessed against a principal or employer for the act of an agent or employee unless such principal or employer authorized or ratified or should have anticipated the conduct in question.

(4) In no case shall punitive damages be awarded for breach of contract.

(5) This statute is applicable to all cases in which punitive damages are sought and supersedes any and all existing statutory or judicial law insofar as such law is inconsistent with the provisions of this statute.

HISTORY: 1988 c 224, §2, eff. 7-15-88

411.186 Assessment of punitive damages

(1) In any civil action where claims for punitive damages are included, the jury or judge if jury trial has been waived, shall determine concurrently with all other issues presented, whether punitive damages may be assessed.

(2) If the trier of fact determines that punitive damages should be awarded, the trier of fact shall then assess the sum of punitive damages. In determining the amount of punitive damages to be assessed, the trier of fact should consider the following factors:

(a) The likelihood at the relevant time that serious harm would arise from the defendant's misconduct;

(b) The degree of the defendant's awareness of that likelihood;

(c) The profitability of the misconduct to the defendant;

(d) The duration of the misconduct and any concealment of it by the defendant; and

(e) Any actions by the defendant to remedy the misconduct once it became known to the defendant.

(3) KRS 411.184 and this section are applicable to all cases in which punitive damages are sought.

HISTORY 1988 c 224, § 3, eff. 7-15-88

Civil Action No. 87-CI-318

WARREN CIRCUIT COURT
DIVISION I

HANSON CONSTRUCTION COMPANY, INC., ET AL., - *Plaintiffs,*

v.

AMERICAN NATIONAL BANK & TRUST COMPANY, ETC., - - - - - - - - *Defendant.*

INSTRUCTIONS TO JURY

In this case, as you know, there are several claims made by the parties against each other, and there are a number of separate issues arising out of these claims. These issues will be submitted to you for your consideration in the form of specific questions, known as Special Interrogatories, which will constitute the form of your verdict.

You should consider all of the following instructions before completing the verdict form to be found at the end of these instructions.

INSTRUCTION NO. I

In this case, one of plaintiffs' claims against the defendant is based upon certain allegedly false and fraudulent misrepresentations made by the defendant, American National Bank, to the plaintiffs, H. C. Hanson, Virginia Hanson, H. C. Hanson Construction Company, Inc. and Construction Engineers, Inc.

The essential elements that the plaintiffs must prove by clear and convincing evidence to establish a claim for fraudulent misrepresentation are as follows:

First, that the American National Bank made one or more of the following representations to the plaintiffs:

(a) That the Bank would provide a new line of credit for $125,000.00 to finance the operation of H. C. Hanson Construction Company, Inc.,

(b) That the Bank would finance the future construction contracts of H. C. Hanson Construction Company, Inc., and/or

(c) That subject to the renegotiation of principal and interest payments at the end of each three-year term, the plaintiffs would have up to fifteen (15) years to repay the American National Bank so long as the plaintiffs paid as agreed under the terms of the restructure agreement and complied with the other terms of that agreement;

Second, that at the time the representations were made, the Bank had no intention of performing them;

Third, that the Bank's representations were made in order to induce the plaintiffs to enter into the restructure agreement;

Fourth, that the plaintiffs justifiably relied and acted upon the representations;

Fifth, that the plaintiffs acted with ordinary prudence in relying upon the representations; and

Sixth, that one or more of the plaintiffs suffered injury or damage as a result of the misrepresentations.

In determining whether the plaintiffs acted with ordinary prudence in relying upon the representations, you will keep in mind that it was the duty of the plaintiffs to exercise reasonable care for the protection of their own interests by making reasonable inquiry or investigation under the circumstances presented.

INSTRUCTION NO. II

In the performance and the enforcement of the loan agreements concerning which you have heard evidence, both the plaintiffs, H. C. Hanson, Virginia Hanson, H. C.

Hanson Construction Company, Inc. and Construction Engineers, Inc., and the defendant, American National Bank, had a duty to act in good faith.

Good faith means honesty in fact in the conduct or transactions concerning which you have heard evidence.

INSTRUCTION NO. III

Corporations such as H. C. Hanson Construction Company, Inc., Constructions Engineers, Inc. and American National Bank can act only through their employees. Therefore, an act of any corporate employee in the course and scope of his employment is the act of the corporation.

INSTRUCTION NO. IV

If you find and return a verdict for the plaintiffs, you will award H. C. Hanson Construction Company, Inc. a sum of money which will fairly and reasonably compensate it for the fair market value of H. C. Hanson Construction Company, Inc. on March 23, 1987, not to exceed $2,130,964.00, the amount claimed.

INSTRUCTION NO. V

If you find for the plaintiffs, H. C. Hanson, Virginia Hanson, H. C. Hanson Construction Company, Inc. and Construction Engineers, Inc. under Instruction No. I, and if you are satisfied by clear and convincing evidence that the defendant, American National Bank, acted toward the plaintiffs with oppression, fraud or malice, you may award the plaintiffs punitive damages against the defendant in addition to any damages awarded under Instruction No. IV.

• • •

The term *oppression*, as used above, means conduct which was specifically intended by the defendant Bank to subject the plaintiffs to cruel and unjust hardship.

The term *fraud*, as used above, means an intentional misrepresentation, deceit or concealment of material fact known to the defendant Bank and made with the intention of causing injury to the plaintiffs.

The term *malice,* as used above, means conduct which was specifically intended by the defendant Bank to cause tangible or intangible injury to the plaintiffs.

* * *

Punitive damages may be awarded against a defendant to punish and to discourage it and others from similar conduct in the future.

If you determine that punitive damages should be awarded, you should consider the following factors in fixing the amount of such damages:

(a) The likelihood at the time the plaintiffs were damage by the defendant Bank's conduct that serious harm would arise from such conduct;

(b) The degree of the defendant Bank's awareness of that likelihood;

(c) The profitability of the misconduct to the defendant Bank;

(d) The duration of the misconduct and any concealment of it by the defendant Bank; and

(e) Any actions by the defendant Bank to remedy the misconduct once it became known to the defendant Bank.

INSTRUCTION NO. VI

Nine or more of you may agree to answers to the questions contained in the Verdict Form. If all twelve of you agree, the answers need be signed only by your foreman. Otherwise, they must be signed by your foreman and by the nine or more who agree to them. If your verdict is not unanimous and is signed by nine or more of your number, and if your foreman is among those who agree to the verdict, he or she shall sign the verdict twice, once as foreman and once as one of the jurors who agree to the verdict.

Any juror may serve as foreman upon being selected by his or her fellow jurors.

VERDICT FORM
SPECIAL INTERROGATORIES

1. Refer to Instruction No. I: Have the plaintiffs established their claim against the defendant for fraudulent misrepresentation by clear and convincing evidence?

YES X NO ___

* * *

2. Refer to Instruction No. II: Are you satisfied from the evidence that the defendant violated its duty to deal in good faith with the plaintiffs in the performance and enforcement of the loan agreements?

YES X NO ___

* * *

3. Refer to Instruction No. III: Are you satisfied from the evidence that the plaintiffs violated their duty to deal in good faith with the defendant in the performance of the loan agreements?

YES ___ NO X

* * *

If you answered "No" to Question 1 and to Question 2, do not answer Question 4. If you answered "Yes" to either Question 1 or to Question 2 and "No" to Question 3, you should answer Question 4.

4. Refer to Instruction No. IV: What sum do you find from the evidence will fairly and reasonably compensate the plaintiff, H. C. Hanson Construction Company, Inc. for the fair market value of the corporation on March 23, 1987?

$1,065,000.00

* * *

If you answered "No" to Question 1, do not answer Question 5. If you answered "Yes" to Question 1 and "No" to Question 3, you should answer Question 5.

5. Refer to Instruction No. V: What sum do you find from clear and convincing evidence should be awarded the plaintiffs as punitive damages?

$5,775,000.00

/s/ Roger D. Crabtree
Foreman

/s/ Roger D. Crabtree
/s/ Jack Butler
/s/ Sandy Whitney
/s/ Barbara Watt
/s/ Orville Phelps
/s/ Norma F. Harvey
/s/ J. Todd Tolbert
/s/ Lawrence White
/s/ Larry LaRue
/s/ Troy Tabor

Credit File

Company name	Person contacted	Company no.
N. C. Hanson Construction Co., Inc.		

7 28

vling Green, Kentucky

☐ Customer ☐ Prospect	Location	☐ In Bank ☐ At Company	Employee no.	Primary SIC no.	Secondary SIC no.	Call date	Follow-up
						/ /	/ /

Subjects Discussed

Credit			Deposit			Cash Management					
11 Revolver	☐N	☐M	21 DDA	☐N	☐M	31 Collection	☐N	☐M	40 International	☐N	☐M
12 Term	☐N	☐M	22 Savings	☐N	☐M	32 Payment	☐N	☐M	50 Trust	☐N	☐M
13 Seasonal	☐N	☐M	23 Time	☐N	☐M	33 Management	☐N	☐M	60 NPC	☐N	☐M
14 Money Mkt	☐N	☐M	24 IRA	☐N	☐M	30 Other	☐N	☐M	70 Lease	☐N	☐M
10 Other	☐N	☐M	25 CTIF	☐N	☐M						
			20 Other	☐N	☐M						

Page no.
1

July 8, 1985

Officer:

Analyst:
T. Gurbach

Background: Subject is a general contractor involved in the construction of bridges, culverts and drainage systems for highways and is owned wholly by H. C. Hanson since 1967. The last five years has seen the company's gross margin drop drastically as highway construction in the state has dropped off, leaving a large supply of contractors and a small demand for work. Thus, Mr. Hanson has been forced to make low bids in order to keep working which has resulted in a net operating loss for the last 4 1/2 years which continuously grows larger. Since 1980 when the situation started to decline up to today ANB indebtedness to Mr. Hanson and related companies has gone from $115M to $707M while debt to other creditors has all but disappeared.

Related Companies: Dixie Engineering (Incorporated - Virginia Hanson, wife - 55%, Stephen Hanson, son - 25%, David Hanson, son - 10% and H. C. Hanson - 10%) is a contractor which Stephen Hanson runs, performing mainly small concrete work. N/was of 5-31-85 was ($26M) and net income for the first six months of 1985 was ($9M). Construction Engineers (wholly owned by H. C. Hanson) is the company Mr. Hanson began with in the contracting business. After his partner died in the late 1960's, Mr. Hanson left this company and started H. C. Hanson Construction Co., Inc., thus this is an inactive company. On 6-4-85 H. C. Hanson Construction Co., Inc., sold Construction Engineers two pieces of heavy machinery for $78M and also transferred $78M of debt to Construction Engineers. This was done so that H. C. Hanson Construction could make a profit on the sale and make its 1985 income statement look better for the bonding company. This company also owns a one-half interest in real estate in Warren Co. (Fred Blaine & Co., owns the other half) which will be mortgaged to ANB under the rewrite.

Purpose of the rewrite is to combine all outstanding of H.C. Hanson Construction Co., Inc., Construction Engineers and Mr. Hanson personally. Following is a list of the above mentioned debt to ANB:

PLAINTIFF'S EXHIBIT
16.

W.H. & C. Hanson Construction Co. Inc. LOCATION: G.

	ASSETS (000's)	Type Data	Unaud 10/31/80	Unaud 10/31/81	Unaud 10/31/82	Unaud 10/31/83	Unaud 1/31/84
1.	Cash		18	46	164	12	
2.	Notes Receivable						
3.	Accounts Receivable, Gross						
4.	Less Loss Allowance						
5.	Accounts Receivable, Net		144	196	176	154	
6.	A/R - Retainage		1	15	17	-	
7.	Inventory		28	31	27	60	
8.							
9.							
10.	Temporary Investment		102	100	100	100	
11.							
12.	CURRENT ASSETS		291	440	484	357	
13.	Land - Other		10	10	10	10	
14.	Land - Co.'s premises		21	14	1	1	
15.	Buildings, Net						
16.	Equipment & Fixtures, Net		316	402	304	223	
17.	Due from Officers/Employees		4	13	12	-	
18.	Prepaid & Deferred Items		8	16	4	9	
19.							
20.	L/R - Affiliate		32				
21.	A/R - Affiliate		54	38	25	5	
22.	Other Assets		11	19	18	19	
23.	TOTAL ASSETS		747	942	860	716	
	LIABILITIES						
24.	Notes Payable, ~~Banks~~ CP - ANB		110	50	31	56	
25.	Notes Payable, Others - LOC - ANB					10	
26.	Current Portion Term Debt - Other		58	44	23	14	
27.	Trade Accounts Payable		71	49	50	96	
28.	Accrued Expenses		16	22	19	15	
29.	Income Taxes		2	-	1	-	
30.	Overdraft						
31.	Due to Subcontractors		56	124	156	25	
32.							
33.	CURRENT LIABILITIES		313	289	280	216	
34.							
35.	Term Debt, ~~Bank~~ ANB		5	253	147	153	
36.	Term Debt, Other		70	36	15	-	
37.							
38.	Subordinated Debt (To FNBL)						
39.	N/P - A.C. Hanson		100	100	100	110	
40.	TOTAL LIABILITIES		488	678	542	509	
41.	MINORITY INTERESTS						
42.	Preferred Stock						
43.	Common Stock		25	25	25	25	
44.	Capital Surplus						
45.	Retained Earnings		234	239	293	182	
46.	(Intangibles)						
47.							
48.	TANGIBLE NET WORTH		259	264	318	207	
49.	LIAB. & NET WORTH & MINORITY INT.		747	942	860	716	

10-450-042 REV 9/84

*24/1

Subject: H.L. AARON CONSTRUCTION CO. INC. — Cash Flow Analysis Worksheet

Statement Date	10/31/81	10/31/82	10/31/83	10/31/84
Net Income from Operations	5	54	(111)	(167)
Items Not Affecting Working Capital:				
Depreciation	79	77	74	84
Amortization				
Deferred Taxes				
Gain/Loss on Disposals	(78)	(129)	(15)	1
Other				
Working Capital from Operations:	6	2	(52)	(82)
(Increase) Decrease in:				
Accounts Receivable	(54)	22	17	(16)
Inventory		4	(54)	16
Marketable Securities				
Other Current Assets			17	
Increase (Decrease):				
Accounts Payable	(22)	1	46	(42)
Taxes Payable	(2)			
Accrued Expenses	6	(3)	5	12
Other Current Liabilities				
Due to Subcontractors	69	32	(131)	(9)
CASH FLOW (DEFICIT) FROM OPERATIONS:	63	59	(152)	(131)
Curr. Mat. of L-T Debt & Cap. Leases at FYE:				
Applications:				
Capital Expenditures	217	4	94	82
Retire Long-Term Debt	74	167		8
Dividends				
Increase Other Non-Current Assets	3	1	16	2
Decrease Short-Term Debt				
Decrease Other Non-Current Liabilities				
N/R- Stkhldr	4			
Total Applications:	303	172	110	92
External Sources:				
Increase Long-Term Debt	214	-	45	177
Issuance of Capital Stock				
Sale of Fixed Assets	77	163	20	14
Increase Short-Term Debt & Overdraft			10	18
Increase Other Non-Current Liabilities				
Decrease Other Non-Current Assets	27	6	35	4
Total External Sources	318	169	110	213
Change in Cash	77	66	(152)	(12)

10-101-637 9/82

55.	Quick Ratio	.72	1.52	1.73	1.63	1.5
56.	Debt/Worth Ratio & (Sub.Debt Adj.)	1.58	2.57	1.70	2.96	1.6
55.	Fixed Assets/Worth Ratio					
56.	Contingent Liabilities Commitments					

	N.C. Henson Construction Co Inc. OPERATING FIGURES (000's)	12 Months Ended 10/31/80	12 Months Ended 10/31/81	12 Months Ended 10/31/82	12 Months Ended 10/31/83	12 Mo Ended 10/31
	[redacted] Revenues	2060	1702	1671	1155	17
58.	Cost of [redacted] Construction	1709	1470	1490	1049	15
	Gross Profit (Loss)	351	232	181	105	1
	Operating Expenses	265	198	199	186	2
61.	Gross Operating Profit	86	34	(18)	(81)	(1
62.	Interest Expenses	45	61	78	59	
	NET OPERATING PROFIT	41	(27)	(96)	(140)	(1
64.	Other Income (Expense)	20	32	151	29	
65.	Extraordinary Gain (Loss)	-	-			
	Income Before Taxes	61	5	55	(111)	(1
8.	Income Taxes (Refund)	2	-	1	-	
68.	NET INCOME (Loss)	59	5	54	(111)	(1
	Cash Dividends/Withdrawals					
70.	Adjustment Retained Earnings					
7	Net Change Retained Earnings	59	5	54	(111)	(1
7	Net Stock Transactions					
73.	Net Change Capital Surplus					
74.	Net Change Net Worth	59	5	54	(111)	(1
7						
76.	Depreciation and Amortization	49	79	77	74	7
77	Percent Gross Margin 59 ÷ 57	17 %	14 %	11 %	9 %	
	EBIT/Interest Expense (61 + 64) ÷ 62					
79	Percent Net Margin 68 ÷ 57	%	%	%	%	
80.	Accts. Receivable Turn 57 ÷ 6 (Days)	26	40	38	50	3
8	Inventory Turn 58 ÷ 8 (Days)	16	8	7	28	1
8	Cash Flow From Operations					
83.	Analyst	T. Gurley				T. Gur

	19			19			19			19			19			19		
	Avg. Coll. Bal.	Avg. Free Bal.	Avg. Loan Bal.	Avg. Coll. Bal.	Avg. Free Bal.	Avg. Loan Bal.	Avg. Coll. Bal.	Avg. Free Bal.	Avg. Loan Bal.	Avg. Coll. Bal.	Avg. Free Bal.	Avg. Loan Bal.	Avg. Coll. Bal.	Avg. Free Bal.	Avg. Loan Bal.	Avg. Coll. Bal.	Avg. Free Bal.	Avg. Loan Bal.

H. C. Hanson Construction Co., Inc.
Bowling Green, Kentucky

H. C. Hanson Construction Co., Inc.

Type	Original Amount	Date	Current Principal Balance	Payment	Collateral	Value
ILD	$ 52,573	01-16-83	$ 21,696	$1,095/Mo.	'83 Ford Truck '84 Ford Truck	$14M
ILD	18,818	10-19-84	12,837	386/Mo.	'85 Mercury	
4 Yr. Term	125,000	02-06-85	119,818	3,323/Mo.	60 ton Crawler #85A	
5 Yr. Term	100,000	10-31-83	100,000	Int Qtrly $20M Principal payment 10-31 of each year	A/R	
5 Yr. Term	125,000	10-31-84	125,000	Int Qtrly $25M Principal payment 10-28 of each year	Equipment	
Line of Credit	125,000*	02-17-84	63,000**	Int Qtrly	A/R, Inv., Equipment	
Letter of Credit	100,000*	06-02-85	0		2nd Mtg. Residence	
			442,351			
H. C. Hanson						
2 Yr. Term with balloon	$175,000	12-30-83	$170,632	$ 2,214/Mo.	1st Mtg. Office $225M the Construction Company operates out of	
Subtotal						
Construction Engineers						
No Maturity Date	$ 78,000	06-04-85	$ 78,000	$ 2,000/Mo.	1980 Komats Dozer	$22M
			$667,983	$12,040/Mo.		

*Amount of commitment.
**As of 7/2/85 the subject has $23M in A/R from jobs in progress and thus the

H. C. Hanson Construction Co., Inc.
Bowling Green, Kentucky

new line will start out with $23M of the old line on it and it will be paid off when these receivables are collected.

The new term loan would be in the amount of $667,983 with monthly payments of $7,594.84 (15 yrs. at 11% with a three year balloon).

This loan together with the letter of credit will be secured by the following:

Description			Value
1st Mtg. Office on Kelly Road			$225,000
2nd Mtg. Residence			187,000
A/R (Receivables on jobs in progress will be used to secure line of credit)			
Retainages		29,000	
Other		5,000	
Doubtful	14,000		
			$ 34,000
Inventory - 2 bridges (one sold for $10M)		27,000	
used materials (he values at $33M)		5,000	
			$ 32,000
Equipment*			
1980 Komatsu Dozer		22,000	
1979 Case Unileader		8,000	
2 1984 Ford Trucks		14,000	
Link Belt - 60 Ton Crane (1974)		85,000	
1969 Bucyrus-erie 20 Ton		15,000	
1979 Ford Backhoe		12,000	
Rustin Bucyrus-erie 150 Tracthoe		20,000	
951C Traxcator (Catipillar) 1972		12,000	
Gromako Slab Machine C450 1981		12,000	
Shield Bantam Motor Crane - 15 Ton 1967		12,000	
Other Equipment (he values at $200M)		20,000	
*Values Come From Last Bid Book			$242,000
Equipment of Construction Engineers			$ 10,000
1st Mtg. One-half Interest - 312 Acres in Barren Co.		13,000	
1st Mtg. One-half Interest - 12 Acres land next to GM in Warren Co.		14,000	
1st Mtg. Lot in Indian Hills		2,000	
1st Mtg. Land in Florida		10,000	
Assignment of CNB Stock		3,000	

H. C. Hanson Construction Co., Inc.
...ling Green, Kentucky

Assignment of H.C. Hanson Construction Co., Inc., Stock & Construction Engineers Stock	0
	$772,000

There will also be a letter of credit for $100M which could be used by his bonding company, Manus & Smith, of Louisville. This would be drawn against only if Mr. Hanson's company was unable, for whatever reason, to finish a contract. This is for one year and will be looked at again after it expires and decision will be made at that time on whether to renew it or not. It will be secured by the above collateral package.

To keep the subject in business ANB will give them a line of credit. This will be used to pay wages for direct labor, or subcontractors, purchase surety bonds and for fuel expense. It will not be used to purchase large beams, etc., as he receives them from suppliers who in turn must wait for the contractee to pay the subject, which will then pay them. These advances will not be permitted until the bank receives a copy of the state's inspector's report (the bank's collateral) showing what percentage of the total contract is completed and the amount he has coming in from the state. When Mr. Hanson receives this payment the entire amount (minus any payments to suppliers for beams, etc.,) will be brought to the Bank and applied to the line of credit. This will insure proper use of the line. Due to the amount advanced will be more than he needs (the difference representing his profit) the remaining will be available for general and administrative expenses, interest on the line and payments on the large amortizing note.

Conclusion: Over the past four and one-half years the subject has lost $387M due to its cutting its gross margin substantially in order to keep working in a very competitive environment. Over the same period the company's and related company's debt to ANB has risen from $115M to $707M as the bank paid for operating and interest expenses that gross profits could not meet and helped retire the debt of other creditors. If the bank foreclosed today it would loose, on an optimistic basis, $140M if the building and land which he operates out of brings its full appraised value at auction and the equipment brings the value the Last Bid book indicates. The loss on a conservative basis would be closer to $250M. Also the $100M letter of credit would be drawn by the Bonding Co., to finish uncompleted jobs, however, the bank would come out alright there as it is secured by a 2nd mortgage on Mr. Hanson's home valued at $190M (note that this is not currently cross pledged with any of the subject's other debt).

However if ANB waited three to five months to foreclose it could come out with no loss due to the taking of additional collateral set out earlier, and due to the subject not having any jobs during the winter, thus the Bonding Co., will not have to draw down on the letter of credit. Due to the restrictive nature of the rewrite no new advances will be made to fund operating expenses or payments of principal and interest on the new term debt when he runs out of contracts this

H. C. Hanson Construction Co., Inc.
Bowling Green, Kentucky

winter, (in previous winters the bank has allowed this, from 6/84 to 2/85 total debt increased $110M) thus this cash will have to come from the sale of his personal assets, in order to keep his company alive. It appears he could sell $18M worth of cattle, cash in a $7M I.R.A. and $5M worth of Kellwood bonds, sell his stock in the B.G. County Club ($2M) or sell some of his household belongings ($30M) over the winter. Other sources of relief would come from the sale of real estate mortgaged to ANB to secure the term note. The money brought in could be used to pay operating expenses instead of applied directly to the term note at the loan officers discretion.

Overall this rewrite should reduce the banks potential loss and force Mr. Hanson to sell off his personal assets which undoubtedly will bring more than if the bank auctioned them off. There is also a slim chance that the demand for building bridges will pick up significantly in the next year or so, Mr. Hanson could start realizing margins of 15%-17% again and pay the bank back through profitable cash flow. However, that is hard to predict and now I recommend the approval of the rewrite and suggest the notes go on non-accrual with all payments reducing principal.

Tom Gurbach Tom Gurbach

TG/40-127

AMERICAN NATIONAL BANK
SWAT MINUTES OF
H. C. HANSON CONSTRUCTION

7-9-85:	We are going to wrap everything together, take all collateral we can get and we should be fairly well secured. We are going to give him a line of credit for this year. We will also be secured by contracts from counties he is working in. We have a $100,000 life insurance policy. Take a good look at this in September to see what his cash flow will be. ($635,706.21)
8-15-85:	All three notes have been combined and additional collateral has been taken. ($691,023.00)
9-17-85:	Loan has been restructured and paying as agreed. Collateral fully covers the indebtedness. ($595,434)
10-15-85:	Loans have been restructured and paying as agreed. ($587,191.61)
11-12-85:	Paying as agreed. The loan is current. ($578,384.79)
12-17-85:	Hanson is dealing with bonding companies for 1986 Bond. Appears ANB will have to extend letter of credit for Hanson to receive a bond of $250,000. The Executive Loan Committee to discuss bonding requirements. ($682,711.35)
1-14-86:	Has been restructured and paying as agreed. ($605,711.35)
2-18-86:	This account has been restructured and paying as agreed. ($696,712.72)
3-24-86:	Continuing to pay. ($603,212.72)
4-21-86:	Paying as agreed. ($606,712.78)
5-20-86:	Has an additional $175,000 line of credit in order for him to sign a contract for a $975,000 job. ($643,212.72)

6-17-86: No change. ($692,212.72)

7-15-87: We have received a letter from Elmo Greer & Sons. They are going to make checks payable to H. C. Hanson, Jim Skaggs, Inc., and ANB. ($691,962.72)

9-17-86: We need to start receiving quarterly financial statements. ($679,890.62)

11-18-86: Received 6 months statement. Continues to pay as agreed. (Need to get assignment on new job.)

1-20-87: He has met with us and reported to have contracted two new jobs totaling $1.5 million. His financial statements will be completed next week and he will be in to negotiate a new escrow line. ($730,000)

2-17-87: On 2-5, the Loan Committee turned down the escrow line of credit. We agreed to fund him an additional three weeks of payroll in order to get contractors to help support company. ($710,476.23)

3-17-87: Demand was made March 11, for payment of escrow lines by April 1, 1987.

4-28-87: Suit filed against ANB by Hanson. In process of countersuit and foreclosure of collateral.

Civil Action No. 87-CI-318

WARREN CIRCUIT COURT
DIVISION I

HANSON CONSTRUCTION COMPANY, INC., Et Al. - *Plaintiffs*

v.

AMERICAN NATIONAL BANK & TRUST COMPANY - - - - - - - - *Defendant*
Counter-Claimant
Third Party Plaintiff

v.

LUCILLE KINSLOW, Et Al

REQUEST TO ADMIT—Filed November 21, 1988

Plaintiffs, Hanson Construction Company, Inc., H. C. Hanson, Virginia Hanson and Construction Engineers, Inc., request that the defendant, American National Bank and Trust Company (hereafter "ANB"), within thirty days after service of this request separately admit, pursuant to Ky CR 36 and for the purposes of this action only, the truth of the following statements:

1. The copy letter dated September 29, 1987, from Gail W. Pohn to Charles D. Greenwell which is attached as Exhibit A is genuine and is a complete and accurate representation of the actual writing which the document purports to represent.

2. Mr. Pohn's conversation with Judge Henry Meigs regarding ANB's consideration of suit against Charles D.

Greenwell and his firm, Middleton & Reutlinger, was intended to influence the representation of plaintiffs in this action by Charles D. Greenwell.

3. The copy of letter attached as Exhibit B is a true and accurate representation of the body of a letter which was sent to the creditors of H. C. Hanson and Hanson Construction Company.

4. The letter to creditors attached as Exhibit B was a proper attempt to verify the claims of creditors and mitigate the damages to plaintiffs resulting from ANB's termination of credit.

/s/ Charles D. Greenwell
Charles D. Greenwell
David J. Kellerman
Middleton & Reutlinger
2500 Brown & Williamson Tower
Louisville, KY 40202
(502) 584-1135
Counsel for Plaintiffs

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the foregoing was mailed by U.S. mail, First Class Postage Prepaid to Darell R. Pierce, Esq., Morgan & Pottinger, 513 E. 10th Street, Bowling Green, Kentucky 42101; Douglas Gene Sharp, Morgan & Pottinger, 601 West Main Street, Louisville, Kentucky 40202; and Robert M. Alexander, Esq., 112 East Public Square, Glasgow, Kentucky 42141, this 27 day of April, 1988.

/s/ Charles D. Greenwell

[LETTERHEAD OF FIRST KENTUCKY NATIONAL CORPORATION]

Charles D. Greenwell
September 29, 1987
Charles D. Greenwell, Esq.
Middleton & Reutlinger
2500 Brown & Williamson Tower
Louisville, Kentucky 40202-3410

Re: Hanson Construction Company v. American National Bank

Dear Mr. Greenwell:

Mr. Doug Sharp has been kind enough to forward to me your letter to him of September 25, 1987, on page 2 of which is noted a conversation that I had with your partner Judge Henry Meigs.

I want to take this opportunity to clear-up, for the record, what appears to be certain misunderstandings or misinterpretations of my conversation with Judge Meigs. It should be clearly understood that in meetings and conversations concerning this lawsuit, I have at all times acted in my capacity as General Counsel to First Kentucky National Corporation, ("FKNC") not First National Bank of Louisville. For your information FKNC is the sole shareholder of American National Bank ("ANB").

In my discussion with Judge Meigs I indicated that ANB was considering filing a lawsuit against you and the firm based on a letter sent by you to creditors of Hanson Construction Company which ANB considers libelous. I further indicated that if we decided to file the suit it would be filed within 30 days. It should be clearly understood that no decision has been made concerning the filing of such a lawsuit either against you or the law firm. The matter is under consideration.

Furthermore, I did not tell Judge Meigs that he should put your firm's malpractice carrier on notice; rather I sug-

gested that he might want to consider such action. I was in no way implying that you have engaged in malpractice in connection with the Hanson litigation. What I did suggest to Judge Meigs and will suggest to you is that the letter written by you to creditors of Hanson Construction Company is defamatory and may be the basis for an action by American National Bank.

It is out of my consideration and respect for Judge Meigs and another member of your law firm, and as a matter of professional courtesy that I felt the firm was entitled to know of this contemplated action.

Should you have any questions or desire to discuss this matter with me please let me know.

Very truly yours,
/s/ Gail W. Pohn
Gail W. Pohn

GWP/29-125

[LETTERHEAD OF MIDDLETON & REUTLINGER]

EXHIBIT B

RE: Hanson Construction Co. v. American National Bank
Warren Circuit Court, Div. I, C.A. No. 87-CI-318

Dear Creditor:

Hank Hanson of H. C. Hanson Construction Co., Inc., has asked me to write you concerning his action against the American National Bank and the efforts being made which we hope will result in the full payment of the indebtedness owed to you.

As with most construction contractors, H. C. Hanson Construction Co. was dependent on arrangements with its bank, American National Bank, for the financing of construction work in progress. For years American National Bank has been the dominant creditor of Mr. Hanson, his wife and Mr. Hanson's companies and held security interests in their respective assets to secure payment of obligations to the bank. Despite past financial reversals, Mr. and Mrs. Hanson and the Hanson companies always made payment on their obligations to American National Bank when due. In July, 1985, after a change in the bank's ownership American National Bank and the Hansons restructured all outstanding obligations to the bank and established lines of credit to capitalize the operations of H. C. Hanson Construction Co. in connection with new work acquired by the company. Mr. Hanson worked diligently to increase his company's work in progress from approximately $250,000 in 1985 to approximately $2.5 million in February, 1987. During this same period, H. C. Hanson Construction Co. went from a reported loss of $125,000 in October, 1985, to a reported profit in 1986. In addition, the Hansons substantially reduced their obligations to American National Bank. Remarkably, however, in February, 1987, American National Bank terminated Hansons'

established lines of credit, demanded payment of Hansons' obligations to the bank and enforced assignments against contract payments for construction work by H. C. Hanson Construction Co., all without any default on the part of Mr. and Mrs. Hanson and the company. As a result, the Hansons have been forced to default on payment of obligations to you and other creditors.

The Hansons' suit against American National Bank maintains, among other things, that the bank's actions violated he bank's duty of good faith and fair dealing in the bank/customer relationship with the Hansons. The Hansons seek recovery for damages including the loss and destruction of H. C. Hanson Construction Co. as a going concern, impairment of credit and reputation and for an amount sufficient to honor the indebtedness owed to you and other creditors.

As part of our proof of damages in this action, I need to have a verified statement of your outstanding account. I would also appreciate a signed statement from you concerning Hansons' credit and reputation with you prior to the present default, i.e., "Hank Hanson and his companies have always had a good credit reputation with me prior to ___."

The bank has responded to the Hansons' suit with a counterclaim for foreclosure on its security interests, including a Writ of Possession against the construction equipment of H. C. Hanson Construction Co. The bank was required to post a bond for $500,000 before taking possession of the equipment and the bond should be available to cover damages if the Hansons prevail in their suit against the bank.

The motives for the bank's actions are not entirely clear. However, discovery is in process and you, or your counsel, are welcome to review the records which we have obtained from the bank. If it is at all possible, Mr. and Mrs. Hanson are anxious to avoid bankruptcy and to honor all obligations which the Hansons or their companies owe. I hope that you will support the Hansons' effort by furnishing the

information that I have requested by way of forebearance on your claim during the course of the pending litigation. Moreover, if you have any knowledge of another case where American National Bank has taken similar action against an established customer, I hope that you will let me know.

If you or your counsel have any questions, please call. In consideration for your patience and upon request, we will attempt to give you a periodic status report on the course of the litigation and the prospects for payment of your claim.

Thank you for your attention.

Very truly yours,

/s/ Charles D. Greenwell
Charles D. Greenwell

CDG:bjh